United States Court of Appeals

for the Second Circuit

APPENDIX

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77-7125 77-7126

United States Court of Appeals For the Second Circuit

DOROTHY L. COLE, LOIS H. ZISOOK, HARRY W. VOEGE and ANNA MAY TUNMORE, as Trustees, SAMUEL GREENFIELD FUND, INC. and HAROLD STILLER and MILDRED STILLER, as joint tenants,

Plaintiffs,

DOROTHY L. COLE, HARRY W. VOEGE, and ANNA MAY TUNMORE, as Trustees, and HAROLD STILLER and MILDRED STILLER, as joint tenants,

Plaintiffs-Appellants,

v.

SCHENLEY INDUSTRIES, INC., GLEN ALDEN CORPORATION, RAPID-AMERICAN CORPORATION, ISIDORE A. BECKER, BERNARD GOLDBERG, PAUL A. JOHNSTON, DAVID A. CHERNOW, WALTER O. HEINZE, HOWARD FELDMAN, MILO B. HOPKINS, RUSSELL G. SMITH, ALBERT N. GREENFIELD, MESHULAM RIKLIS, GLEN ALDEN SUBSIDIARY, INC., P.J. CLIFFORD, W.P. JOHNSON, S. KITTAY, M.L. MENDELL, L.C. LANE, G.H. PERKINS and B. DENMARK,

Defendants-Appellees.

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(Volume II—Pages A324-A657)

HERMAN ODELL
Attorney for Appellant
Dorothy L. Cole
460 Park Avenue
New York, N.Y. 10022

Dick Bailey Printers, 290 Richmond Ave., Staten Island, N.Y. 10302
Tel.: (212) 447-5358

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A No.

Q Was cash generated in Schenley pursuant to a program?

MR. SILVERMAN: Objection, your Honor.

THE COURT: No, overruled. Let's find out.

A In the normal course of business.

Q Was it pursuant to a program was my question.

A In the normal course of business.

Q Yes or no, was it pursuant to a program?

MR. LEVIN: I object, if your Honor please.

THE COURT: Sustained. The word "program" is giving us problems.

Q Did you ever testify that you had -- that $200 million in cash was generated pursuant to a program?

A You are quoting the fact that I have said the $200 million was generated including the sale of Buckingham, which was not a part of the thinking in 1968 when the company was purchased. In addition to which there were over $40 million of earnings retained in the business. This is all part of normal business procedure.

Q Was it part of your normal business procedure to accumulate this amount of cash?

A I don't understand what you are trying to say. It was all done in normal business procedure.

Q I'm not saying it is legal. I'm just asking whether you at any time said to your management, I want a program instituted to generate cash, to generate as much cash as we can.

A I believe I have answered that question yesterday when you asked me and I said I wanted cash generated in order to produce the highest earnings in the least amount of invested capital.

Q Did Glen Alden have any difficulty raising new money as distinguished from refinancing their old -- their existing debts in 1970 or 1971?

A I don't believe Glen Alden had any problems raising almost any amount of money because of the -- its relationship, its assets, its ownership and control of companies was such that it had sufficient assets to almost raise any amount of money within reason to that particular corporation.

MR. ZULACK: Thank you, Mr. Riklis.

THE COURT: You may step down.

(Witness excused.)

MR. ZULACK: Your Honor, I would like to make an offer of proof as to the 1972 Hayden, Stone --

THE COURT: Let's wait until you get your witness up here and we see where we are at. What would you like to

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do. Mr. Odell, do you want to put in these exhibits?

MR. ODELL: I would like to try to put them all in.

THE COURT: Have you talked to your adversaries about what they are?

MR. ODELL: I mentioned to them this morning.

THE COURT: Why don't we take a nice 15-minute recess at this point and you and your adversaries look at these exhibits.

MR. ODELL: May I suggest that we will not need Mr. Chernow at least until 2 o'clock. He is my next witness.

THE COURT: Who will you go on with after the exhibits go in?

MR. ODELL: Mr. Chernow. He is here now.

THE COURT: If the exhibits go in evidence, suppose we take a half hour to put them in and rule on objections. We are then at noon with an hour to go before lunch.

MR. ODELL: Let's see how we do on the objections.

(Recess)

MR. SILVERMAN: If your Honor please, the defendants have canvassed among themselves with respect to an orderly and hopefully expeditious procedure for coming to grips with the exhibits and we think that it probably would

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2 be time-saving in the long run and the consistency of rulings
3 would be in a sense enhanced if we did this list one by one
4 because, and I just do this for the sake of illustration,
5 there are an enormous number of exhibits which could be intro-
6 duced, for example, under the business records rule, but our
7 problem is that as we have viewed this case, it is a proxy
8 case and not a fairness case. We would therefore object.
9 What troubles us is that if we put so many of
10 these things in for whatever they may be worth, we are going
11 to be litigating this case as a fairness case in briefs and
12 that, in a sense, puts us at an enormous disadvantage because
13 we did not look upon this as a fairness case and if it is,
14 we have to put in a fairness case to rest only on this material
15 without knowing whether it is a fairness case or not would
16 be troublesome to us.
17 I think as our objections unfold to specific
18 documents and your Honor's rulings on them will in a sense
19 inform everybody as to what this case is about and your Honor
20 may then accept or reject such exhibits as you are wont to
21 do. I do think it would save time if we did it one by one.
22 THE COURT: Let me ask you this. I have got work
23 going on on whether fairness is in this case or not and I
24 have been troubled by the awareness that I was going to reach
25 that issue at a time when I was not quite yet prepared to

reach it. I would rather not reach it on a wholesale level, which I apparently will have to do if I am going to rule on 25 or 50 exhibits.

MR. SILVERMAN: A hundred and some-odd.

THE COURT: A hundred and some-odd exhibits.

Is it possible to go forward with the testimony of our next witness, which will give me the lunch hour to give me time for further consideration of that issue and reach this issue later today? In other words, the next gentleman that you have in mind we can take him, I assume, virtually in toto without necessarily having to squarely confront the fairness issue; is that so?

MR. SILVERMAN: I am perfectly willing to go forward with Mr. Chernow.

THE COURT: And can that be done without handicap to you on the plaintiffs' side with regard to whatever documentation you are going to want to present to him?

MR. ODELL: Your Honor, I am troubled by several things Mr. Silverman said. The fairness of this merger is in the pleadings. It is out in full bloom in the pretrial order as one of the issues --

THE COURT: I know, but he takes the position that once, as I understand it, the position of the defendants collectively as enunciated by Mr. Levin was that once you

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2 have -- you can put it in the pleadings which raises the issue

3 and you go to bat on that issue on the motion for a pre-

4 liminary injunction. Correct me if I am wrong.

5 MR. LEVIN: That is correct.

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THE COURT: If you lost that, you have lost that as an issue for ultimate determination being relegated only to appraisal or going along with the deal or one other that I can't remember --

MR. LEVIN: Provided there is no disclosure problem.

THE COURT: Provided you have no disclosure problem.

You are left with your disclosure issues or your client's right of an appraisal, but you have lost the right to litigation of the fairness issue, certainly in the federal court.

Mr. Levin, I think, said to me he knew of no case -- and I assume that able attorneys in several offices were looking for them -- he knew of no case where any federal court had had before it after trial, an issue of fairness such as to set aside --

MR. LEVIN: After merger.

THE COURT: -- after merger had a fairness issue.

MR. ODELL: No federal case?

THE COURT: That is what Mr. Levin said.

MR. LEVIN: That's what I said, in addition to which there is the pending jurisdiction question. If there is no disclosure problem to which anything would attach,

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The only cases that I know about on the question of pendent jurisdiction is where a federal claim on the pleading is dismissed out of the case with nothing left, nothing more left in the case than the common law case.

At that point, the basis for pendent jurisdiction has disappeared but having gone through months of discovery, practically years of discovery and all the laborious procedures that we have experienced in this case and come to trial without having had the federal claim dismissed or even any question raised as to --

THE COURT: There is question raised as to it being thoroughly litigated. It is going to be thoroughly litigated.

MR. ODELL: What I am saying is, if the federal claim is not dismissed in advance of trial, a number of courts have said it is sound exercise of discretion on the part of the trial court and I will be glad to give you some of the cases -- we have them here with us -- that the common law cases should be -- the common law claim should be adjudicated even if the federal claim is found not to have merit.

There are even cases that say that you can -- on a motion for summary judgment if the federal claim is dismissed, as a matter of discretion so long as there is

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then your Honor is without --

THE COURT: Then the balance of it falls away unless by some major exercise of discretion you wanted to hang on to something because you had done all the work and saw no reason to give it to somebody else.

MR. LEVIN: That's why we believe, your Honor, we are obliged to raise this issue at the very outset.

THE COURT: This is the Gavit doctrine which says you can hang on to it even given all else, but you probably ought not to.

I am at work to ascertain whether, therefore, as a matter of law, your fairness issue is before me or is not before me. It may well not be before me if your adversaries are right.

MR. ODELL: In the first place, it seems to me the law is quite clear there is a matter of pendent jurisdiction and the number of federal cases on that question that having advanced this far into trial, that the questions of the common law case, so long as they have a common nucleus of facts with the federal case, are as a matter of convenience and justice and time of the parties concerned to be litigated in the federal courts.

There have been a number of recent cases that say that in the federal court.

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that common nucleus of facts, that common law claims can be litigated in the federal court.

This is an important question, your Honor. I haven't tried to answer what Mr. Levin said here in the course of an argument but it seems to me if your Honor is going to pass on that question at lunchtime and make this kind of decision, we ought to be able to be heard on this question and it ought to be briefed and argued with a lot more time given to it than Mr. Levin would like us to have here.

THE COURT: I thought he not only raised the issue fairly squarely in his argument but I remember even quizzing him about it to make sure I had the argument clearly in mind.

MR. ODELL: I don't question that, your Honor. All I am saying is we haven't had a chance to respond to it and I think as a matter of pendent jurisdiction, if for no other reasons, the common law claims at this stage in this litigation against this backgroundare in this case.

THE COURT: The common law claims constitute what?

MR. ODELL: The merger terms were unfair.

THE COURT: When you say common law claims, you are talking about the fairness claim?

MR. ODELL: Fairness of the merger.

THE COURT: All right. Let me throw one more question into the hopper, which is, what weight am I required to or should I give to a determination in Delaware as to these terms? None?

MR. LEVIN: If your Honor please, on the question of pendent jurisdiction, our position is there is not state claim. Judge Marvel in this case, and I think it is uncontradicted that insofar as Delaware is concerned, the exclusive remedy is appraisal.

THE COURT: I know but that's what I am getting at. There has already been an appraisal proceeding that is now on a second appeal, a second level of appeal from a master's report.

MR. SILVERMAN: Yes, sir.

THE COURT: I'm not to blind myself to that fact either.

Isn't that a determination in the fairness area that is a further incidence of why should I get into something where the state court, which is the proper place for it, has already done it?

When I say, what weight do I give to that --

MR. SILVERMAN: That's precisely our position.

THE COURT: Your brief, Mr. Odell, never spoke at

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all, your pretrial memorandum never spoke at all to what effect I should give, if any, to these proceedings that have already taken place.

Your memorandum -- correct me if I am wrong -- your memorandum proceeds on the theory that nothing ever happened outside of this very numbered litigation that is before me.

MR. ODELL: Your Honor, I did refer to the result in the state court case --

THE COURT: It seems to me if there has been a determination in the proper forum on fairness, that's a factor that I ought to give some weight to, even apart from the pendent jurisdiction question that faces me.

MR. ODELL: I think if your question is, is the result in the state court either res judicata or a basis for collateral estoppel as to what the fair value of this stock is, I would say that the authorities are certainly not clear on that question, and I'm not really advocating that position for the very reason that Mr. Silverman gave here earlier when he described the peculiar nature and the ground rules that apply with respect to arriving at value under the Delaware appraisal proceedings.

I do say to your Honor that you can't put the blinders on, nor can anybody else, that a court has decided

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in that case under very limited evidence that the stock was worth more than was given to it.

The second thing I have to tell you is the only people involved in the appraisal case were some 200,000 shares of this 3,600,000 shares. The other people -- there were no other parties to that case.

That result is not binding on anybody else that is not a party to it.

THE COURT: No, but you are asking me to take pendent jurisdiction over the subject matter of something that has already been litigated in Delaware, which is the right place to litigate, in the first instance.

MR. ODELL: Your Honor, there are any number of cases that say, even in the Delaware courts where you have a merger between a parent and a subsidiary, that appraisal is not the exclusive remedy --

MR. SILVERMAN: No, sir.

MR. ODELL: -- that appraisal is not the exclusive remedy. Those are the cases he is talking about.

I believe the only time appraisal might be the exclusive remedy in Delaware on an unfairness case is where you have a merger between a parent that owns 90 percent or more of the stock of a subsidiary, and in no other type of case.

The short form merger --

THE COURT: Mr. Odell, let me ask this. As I said many times, and it is going to be true throughout this case, you gentlemen have lived with this case until it has seeped to the roots of your hair.

MR. ODELL: It certainly has.

THE COURT: I have not, and therefore, you have got to give me all the assistance you can.

I would assume that in the state court in Delaware, somebody claimed in an appraisal proceeding that the $29 figure was, quote, unfair, quote.

Was that raised?

MR. ODELL: Yes.

MR. SILVERMAN: Yes.

THE COURT: I assume you did have an opportunity to participate in that proceeding, whether or not you chose to do so.

MR. ODELL: No, we had no opportunity for this reason:

The Delaware appraisal statute establishes certain prerequisites to becoming a party to an appraisal proceeding. You have to do certain things. You have to object. You have to submit your stock to be marked.

THE COURT: Your clients could have done that but

chose to travel a different route.

MR. ODELL: That's right.

THE COURT: All right.

MR. ODELL: The other thing --

THE COURT: Let me follow this up. Since that has been litigated by some people who are members of the class, if I can use that word loosely, why should I litigate that point a second time even as a matter of pendent jurisdiction?

MR. ODELL: Well, the first --

THE COURT: You are looking, obviously, for a different result from me than you got in Delaware.

MR. ODELL: Your Honor, a lot of this question of people in the appraisal case was raised in the definition of this class in extended arguments before Judge Weinfeld.

The first thing Judge Weinfeld said was that when you come in under a federal remedy like the Securities and Exchange Act of 1934, your remedies are not in the slightest to be prejudiced, shortened, reduced or in any way adversely affected by what the state law provides, and Judge Weinfeld included in his definition of the class in this action, those people who sought appraisal.

I am saying that to indicate that there is

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nothing in the appraisal proceeding or in anyone going into that appraisal proceeding and only those people who are parties and become parties by a number of deliberate acts that have to be taken by each stockholder, those are the only people who are bound by that appraisal proceeding.

Now, we visualized at the time that conceivably the appraisal could result in a judgment that the merger terms were fair or that the stock was worth $5 more and because of the peculiar rules of appraisal proceedings and their methods of appraisal as established in Delaware, that someone with the federal remedy could have a claim for as high as $40 or $45, and what do you do with the fellow who sought appraisal and got $4?

Our position was, and apparently accepted, that if you got $4 there and the result here was that the stock was worth $40, he would get the difference between 33 and 40, having received what the appraisal proceeding awarded.

So that I don't see that the appraisal proceeding, anything that was done in the appraisal proceeding, considering the peculiar nature and the limited jurisdiction of the court in the appraisal -- it is not a class action, your Honor, and nobody -- the only members of this class --

THE COURT: It is provided by the law in the state of incorporation which applies to this very class of

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securities so when you say it is a limited jurisdiction, it is the jurisdiction for someone buying into this corporation, limited or not.

MR. ODELL: Your Honor, my answer to that question is that the Delaware courts have not held, and the Delaware Supreme Court has not held that appraisal is an exclusive remedy.

Where the terms of a merger are unfair and are demonstrably unfair --

THE COURT: Let me put another question to you:

Is there any question here that your common law pendent jurisdiction claim is one that it is in the discretion of this Court to keep or reject? Is it mandatory that the Court keep it or is it a matter of discretion that the Court keep it?

MR. ODELL: I said it was a matter of discretion and I said in view of some recent cases that have tested the degree and the basis of the discretion that is exercised, that where you go through a whole pretrial preparation and all the time is spent and come to trial and if as a matter of pleading, your federal claim is not dismissed as a matter of law, that in the exercise of sound discretion, the court can and does and will exercise pendent jurisdiction to hear the federal claim as long as there was a common nucleus of

facts and I think we have that common nucleus of facts.

It has to do -- your Honor, there would be no disclosure case here, really, if the disclosure that was complained of did not relate to the value of the Schenley stock because that was basically the main decision that a stockholder asked to vote on this merger had to make a decision about.

If that was -- if there was any lack of adequate disclosure with respect to the terms --

THE COURT: In effect you are saying it is -- then there is no --

MR. ODELL: I'm trying to show most of what we are trying to prove is that they failed to disclose the facts that related to the fairness --

THE COURT: No, if I can quickly go around the corner of this barn, doesn't that affect every document that you propose to put in evidence, that they can all go in on the disclosure theory? Because you say they are co-extensive.

MR. ODELL: Your Honor, I would say so and I would say another thing:

I don't think there are many documents here that relate solely and exclusively to fairness as distinguished from disclosure.

THE COURT: Let me hear from the other side. Mr. Silverman behind you has been bobbing up and down bursting to oppose certain things you said. Let me catch him when he is fresh.

MR. SILVERMAN: So many things have been said. I will try to pick them up.

In the first place, this is a disclsoure case and it is the facts that we are dealing with in terms of disclosure.

My friend, I don't believe -- it is not a case that says you did not say this was unfair. That's not what he is saying. He says you did not set forth the facts from which stockholders could make reasoned decisions.

The facts that he says should have been disclosed as opposed to conclusions and whatever, we have no objection, that is the stuff of a proxy case.

What we say is that the disclosure case, the proxy case, the 10(b)(5) case, whatever the denomination of it is, is all that is triable in this court.

THE COURT: Let me ask you for some guidance, Mr. Silverman.

It would seem to me, perhaps I'm wrong, but it would seem to me the teaching of that Abramson case, with which I have some familiarity, was that even if the terms

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were "unfair," as long as you had spelled the whole thing out, it was not up to the shareholder -- the shareholder had no right to complain as to the unfairness in a federal case. He could, upon being informed of the facts, he could reject the proposal as far as this Court is concerned.

MR. SILVERMAN: That's right.

THE COURT: All this Court is concerned about is does he have the facts before him so he knows whether to accept or to reject the proposal.

MR. SILVERMAN: Precisely. And that is the teaching of not only the case which your Honor cited but there are other cases in this Circuit, in this District, which come to the same conclusion.

Now, if once you are satisfied, if you are, that there has been adequate disclosure, that ends the federal case.

Now, my friend says, as I understand it, that you then have to go forward and try what he considers to be a pendent jurisdiction case.

There are several -- first, there is a broad caveat, or at least I would dissent to this extent:

The implications of what my friend says are, you can posit a state court case and if you will then make an allegation sufficient to bring you into this court, an

1 15-1zesb

2 allegation which is not dismissible before trial, you can
3 import everything from across the street into this court
4 if you will just make the appropriate allegations because
5 if it isn't dismissed before trial and there are
6 allegations that I could posit in any case that are not
7 dismissible before trial, you are home free, this court
8 becomes a companion court to the court across the street.
9 That is the philosophical problem that I have
10 with my friend's formulation but now let's horn in on this.
11 What is pendent jurisdiction? That is, what is there that
12 remains to be tried, assuming that there is no failure of
13 disclosure.
14 The only remedies that exist under Delaware law,
15 and we are a Delaware corporation, for a stockholder to
16 build in the state court, which is the pendent jurisdiction,
17 is the appraisal remedy.
18 My friend says that I am wrong on the law.
19 I will cite you to this very merger where
20 Chancellor Marvel said when an attempt was made to enjoin
21 this merger because every stockholder has a right if he
22 believes there is unfairness, overreaching,or whatever, to
23 go into the state court and say, stop it, it is unfair.
24 Judge Marvel or the Vice Chancellor Marvel said,
25 "It is not unfair on the application for an injunction.

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There may be a difference of some small amount. You may consider that you have not been adequately paid. What, then, is your remedy if I denied your injunction?" And he said --

THE COURT: Where are you reading from?

MR. SILVERMAN: From page 52 of our brief. But I have furnished the full opinion of Chancellor Marvel to your law secretary.

THE COURT: Go ahead.

MR. SILVERMAN: "Unless the fair value of Schenley's stock is so much greater than the total amount offered, then it would appear that the parties are merely in dispute as to value for which an appraisal should be adequate.

"If plaintiffs and others are not satisfied with the value placed on their shares by Glen Alden and no fraud or blatant overreaching is demonstrated, their recourse is to an appraisal."

That is the state remedy. Since that remedy, for those who under Delaware law, which indicates what the access to their courts will be, since those proceedings have already begun, and my friend has chosen not to take advantage of them, he has no state remedy now.

He has chosen to come to the federal court on a disclosure case and we are not going to deal with the measure

of damages if he is successful because your Honor has put that off, but if he fails in his disclosure case, he is finished, we respectfully submit.

Now to be more practical about this, because your Honor is obviously considering this submission and I don't think anyone wants to push your Honor into a quick and perhaps an -- not adequately studied decision, I would propose that we do what I thought we were going to do.

The first part of this case will be a trial of the disclsoure issues.

The s[illegible] part, if your Honor at that point decides that there is -- my friend has succeeded in that -- the second part of the trial will be damages which, in a large sense, we will be debating the fairness issue.

If your Honor, however, at that point says, no disclosure problem at all, there is adequate disclosure, it will be at that time that your Honor can then make his decision as to whether we go forward in the second phase of this trial on the issue of fairness.

Our stipulation and your order said that if matters with respect to fairness necessarily come in in the disclosure case, nobody will have to remove them or put them in again and it seems to me that that is a thoroughly sound, workmanlike way to proceed without a hiatus in the

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trial so that your Honor can consider our submission and yet have the trial go forward on what we suggest is the issue, i.e., adequate disclosure.

THE COURT: Well, let's go forward, certainly, now with your next witness who is here and ready to testify.

MR. ODELL: I know what Judge Marvel said in his opinon. It was an application for a temporary injunction and pointed to the adequacy of monetary damages and since there didn't appear to be such a violently than fair merger from the face of things as he saw it based on market prices, and so on, he denied an injunction.

It is my position that the Supreme Court of Delaware has said on more than one occasion that what Mr. Silverman or what Judge Marvel said by way of dicta is not the law in Delaware and the Supreme Court of Delaware has not reversed its previously announced principles dealing with when and where and under what circumstances you need not go to appraisal and you can come into a common law court, a court of chancery in Delaware.

And where you show that the terms of a merger are so palpably unfair in terms of values as to demonstrate or indicate a lack of good faith on the part -- and I'm talking now primarily of parent-subsidiary mergers -- that where you can demonstrate a lack of bad faith in fixing the terms of

2 the merger, a Delaware court will give you relief and the
3 way the court talk is, these merger statutes were not
4 designed to permit somebody to get away with murder in terms
5 of depriving people of the value of their stock.
6 THE COURT: Let me just quickly sum up where I
7 feel I'm at and then you will have some guidance.
8 It seems to me that where this Court has denied
9 a preliminary injunction, where a court in Delaware has made
10 a finding that the terms were not unfair, that it is
11 inappropriate for this Court as a matter of discretion to
12 re-litigate the fairness issue as a fairness issue and this
13 leaves in clear outline the disclosure case which obviously
14 everybody is eager at this point to get forward with and try.
15 That is in a nutshell where I feel I'm at. I
16 am leaning towards saying that fairness is not going to be
17 an issue before me on this trial because it has been an
18 issue under other circumstances that make it inappropriate
19 for it to be an issue before me.
20 I am prepared to hear anything to the contrary
21 that you want to submit to me. I do not have a closed mind
22 but I have a leaning body, all right.
23 MR. ODELL: Your Honor, we all have leaning
24 bodies. All I am asking is to be heard on that question at
25 length and fully.

lzesa

THE COURT: Why don't we put on this next gentleman who is waiting to testify here. I gather you can take his testimony without in any sense raising head on the issue of fairness or unfairness?

MR. ODELL: It is hard for me to say that, your Honor.

THE COURT: Well, you have said to me that the disclosure case is really the fairness case. That is what you said a minute or two ago with almost no exceptions.

MR. ODELL: No. What I was trying to say is the failure to disclose facts bearing on the value of the stock that an investor ought to have is the disclosure case. And in order to prove that case, you have got to show that these things relate to the value of the stock.

THE COURT: Absolutely. I understand. So does all counsel. And to the extent that you do have a gentleman here now who is prepared to testify, I assume to facts which would be equally applicable to either the disclosure or the fairness issue, therefore, there is no question we can receive his testimony completely on the disclosure issue and if it later becomes as applicability to fairness, it will have such applicability.

MR. ODELL: Your Honor, I'm going to do my best to try to follow the outline you gave me.

lzesb

THE COURT: Very good.

MR. ODELL: If I lapse in doing so, you can slap my wrist.

THE COURT: No, I will appreciate the problem you are up against and we will keep going.

Sir, come up.

MR. ODELL: Your Honor, I must tell you that I was hoping for a different disposition for the admission of these records. It may take a minute or two to get the exhibits. If you will bear with me, I will appreciate it.

THE COURT: No problem.

D A V I D A. C H E R N O W, called as a witness by the plaintiffs, being first duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. ODELL:

Q Mr. Chernow, when did you first become associated with Schenley Industries?

A In 1954 as an employee.

Q When did you first become an officer of Schenley?

A In 1958.

Q What office did you then succeed to?

A Vice president of Schenley Industries.

Q Did you have a particular area of responsibility

as such a vice president?

A Up until that time, I was involved as executive assistant to the president of the chief marketing arm of the company.

In 1958, I was, at the time of my election to vice presidency, assigned to the financial portion of the business.

Q In that financial portion of the business, would you tell me what particular areas of your concentration were?

A I was involved with our relationships with distributors in terms of their accounts. I was involved with our financial institutions and was involved with the activities relating to our investments in assets of the company, inventories and the like.

Q The distributorships you referred to, would you explain that briefly to the Court?

A The channel of distribution in our industry is that we, as a distiller, sell to either a franchised or non-franchised distributor in a particular market. He, in turn, sells to the retailer, who, in turn, sells to the consumer.

Q Did there come a time after 1958 when you were made what was then called the financial vice president of Schenley?

A Yes.

Q Would you tell us when that was and what change in duties occurred when you succeeded to that title?

A In 1965, I became vice president, vice president-finance of the corporation. With that title came the additional duties of direct responsibility for the controller or the accounting functions of our business as well as more direct involvement with our financial institutions, our commercial banks, our insurance companies in connection with direct financing.

Q So that as far as the financial end of your responsibility was concerned, is it fair to say that you were the man in Schenley with the primary responsibility of dealing with those banks and other institutions that lent money to Schenley?

A In 1965 on, that's correct.

Q And from that time to almost this day, since I haven't talked to you recently, that has been the area of your responsibility in Schenley?

A My responsibilities have recently been expanded beyond that.

Q Without arousing any flak, let's first find out when was the first time they were expanded.

I believe you had testified previously that

sometime in 1969, you were made an executive vice president?

A Yes.

Q Is that so?

A That was so at that time.

Q Tell us in what respects your duties as an executive vice president were expanded over what they had been previously.

A In that function, the administrative operations, administration of our company's activities and departments also reported to me.

Q You got to February of 1969 where you assumed these additional duties.

Is it accurate to say that in these duties you assumed in 1969, that the vice president and treasurer of Schenley -- the vice president and treasurer of Schenley reported to you?

A It is.

Q And that the vice president in charge of administration of Schenley reported to you?

A It is.

Q And between those two main categories of responsibility, administration and finance, there was within your area of responsibility a primary responsibility, all the internal accounting functions that were performed by

Schenley, is that correct?

A I think I have indicated that, yes, sir.

Q And Schenley did have an organization that discharged all of the internal financing accounting problems or duties that were inherent in the organization?

A Yes.

Q And did your area of responsibility include those departments of Schenley that dealt with the vital statistics of Schenley, such as case sales?

A Through the organizational structure, those units would have eventually, or through their structure, reported to me.

Q And would those statistics dealing with gross profits and marketing profits and -- gross profits, marketing profits of, say, the case sales activities of Schenley, were those statistics within the area of your responsibility?

A Through one unit or another, yes.

Q Would you tell us what your responsibilities and dealings were with the auditors of Schenley? Were you the man that dealt with the auditors who came in periodically reviewing the books and records of Schenley, who came to you concerning questions they had?

A As a normal practice, the outside auditors dealt

with our assistant comptrollers and when they would come to a conclusion or if there were an issue that might need further resolution, I would sit with our assistant comptrollers and the auditors to attempt to resolve whatever situation was under discussion.

Q Well, is it fair to say that anything beyond a routine or a question involving a small amount of money in terms of an auditing procedure, that is it fair to say that in the larger matters affecting the auditing procedures, they were generally brought to your attention?

A Larger matters were brought to my attention, yes.

Q Did you perform any functions in terms of scheduling the production of new whiskeys by Schenley?

A I was involved in that, yes.

Q Would you tell us what those functions were?

A At what period in time?

Q Let's take them, say, two years beginning 1966.

A Beginning 1966? During that period of time and now, you have a different series of functions in which I was involved in when you talk of 1966.

Q Well, just tell me simply --

A I was not at that point in a decision making position relative to the production of new whiskey.

Q Well, were you in a statistical gathering or

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analysis situation?

A Not at that point in time.

Q In other words, you had no responsibilities to speak of in respect to --

A I had full awareness of it but no direct responsibility with --

Q In connection with your financial responsibilities, wouldn't you have to know how much new production was being scheduled each year so as to make sure that the funds necessary for that production were budgeted, borrowed, obtained and provided as necessary?

A Knowledge of it, yes, but not determination.

Q To that extent, you were familiar with the new production activities of the company because they required financing and budgeting activities that were important to the system of controls that you were administering in this corporation, isn't that right?

THE WITNESS: Would you give me the question? It got a little distended there, I think.

THE COURT: Read it back.

(Question read.)

A I had knowledge of them and to that extent, it was right.

Q All right. Did there come a time after 1966 when

2 your decisional responsibilities expanded with respect to
3 new production?
4 If they did, say so and tell us what the nature
5 of that expansion was.
6 A Yes. In the fall of 1968, I became more directly
7 involved with the final determination of what and how much
8 would be produced of various bulk whiskeys which were the
9 substance of our case sales.
10 The detailed analysis of inventories on hand,
11 production capabilities were all prepared by other
12 individuals. The vice president of manufacturing was
13 involved in that. Our bulk whiskey utilization manager was
14 involved in that.
15 Then they would sit with me and we would review
16 what would make sense for us to produce in the following
17 production season. This was a pattern that we attempted to
18 review every three months as possible changing consumption
19 patterns became apparent to us since we had to project for
20 usage for quite a number of years ahead.
21 Q Would you tell us what your responsibilities were
22 in the area of decision making with respect to sales in bulk
23 of Schenley stores of whiskey, and would you before saying
24 that --
25 THE COURT: Before you get there, I gather that

you are bottling for a potential drinker six years ahead, is that right?

THE WITNESS: We distill for the potential drinker and we put it in a barrel particularly or specifically as it relates to Bourbon whiskey or bottle in bond whiskey or blended whiskey to a certain portion of its component.

THE COURT: What happens if you made a mistake, there it is?

THE WITNESS: Well, there are several types of mistakes you can make.

You can produce too little and if your brand in that intervening time becomes a hot brand or very popular brand, you have, in effect, lost the benefits of all your advertising because for many brands, you cannot use somebody else's whiskey or whiskey produced for another brand.

If you produce too much, you either look for a buyer or you attempt to use that whiskey in another brand or series of brands.

So that it is a constant process. It is not a decision made in a moment in time, put away in a drawer and wait for a final evolution.

THE COURT: Sorry I derailed you.

MR. ODELL: Your Honor, derailments are a common

2 thing in good statements, so I will go along.

3 BY MR. ODELL:

4 Q I was getting into the question of sales of bulk

5 whiskeys as distinguished from whiskeys that were in bulk

6 and then were transformed for use in cases for manufacturing,

7 put in cases.

8 Did you have any responsibility with respect to

9 bulk sales of whiskey by Schenley?

10 A I was aware of it and would generally either by

11 myself or in conjunction with the president of our company

12 approve of such a bulk sale as they came about. Bulk sales

13 are sometime things. They are not day-to-day.

14 Occasionally someone else will need bulk whiskey

15 and we will learn of it, and so it was the kind of a

16 situation that happens only from time-to-time.

17 Q Well, but within the area of your responsibility

18 in scheduling new production of whiskeys, wouldn't those

19 decisions relating to scheduling be affected by the volume

20 of bulk sales?

21 In other words, if you sold or plan to sell more,

22 you might produce more. If you planned to sell less in bulk,

23 you would produce less.

24 Wouldn't there be an interrelationship between

25 bulk sales --

A Many factors are interrelated and we can't put a priority on one as dictating our course of action on the other. They were all interrelated and certainly we took them all into account.

Q Mr. Chernow, I am not trying to oversimplify the important functions you performed. I am trying to point out that is one of the many things you took into account. Let me just ask a few more questions apropos of what the Court asked you about.

You stated -- well, in the first place, all the bourbons and straight whiskeys produced by Schenley were aged a minimum of four years, is that correct?

A In order to be called bourbon whiskey, you have to it aged at least two years. However, we and the rest of the industry used four years as a minimum criteria for it.

Q I'm not trying to pin you down to an exact figure but within the complicated procedures and the uncertainties that you have described that were involved in the process of scheduling the amount of new production, was there some sort of rule of thumb that you used in planning ahead?

In other words, were you trying to get an average of six years' current sales or five years' current sales as being the total amount of your bulk inventory?

2 A In dealing with a bulk inventory, you cannot
3 deal with it in the aggregate. You deal --
4 Q Let's deal with bourbon.
5 A Not even bourbons. You deal with it as a single
6 brand because you distill bourbon with an intention of its
7 utilization in a single brand.
8 If it is your projection that five years from
9 today on the brand which carries a five-year age statement
10 that your sales are going up at a rate of 5 percent a year,
11 you better be in a position today of planning 25 percent
12 more production so that you will have it five years from
13 now, subject, of course, to further modification as you make
14 your further views.
15 Q So just on the example you gave, if you were
16 planning the production of whiskey for a four-year bourbon
17 label and you saw sales increasing at something like a
18 5 percent rate per year, you would, in effect, be planning
19 for, say, twenty-five to thirty percent more than what you
20 were selling in the year you planned that production?
21 A That would be so.
22 Q So that in overall terms in using your rule of
23 thumb, you would say in planning the inventories you would
24 need for a four-year old brand, you would roughly plan for
25 the equivalent of six years sale, wouldn't you, enough to

2 cover you six years to date?

3 A I don't see that.

4 Q You said 25 percent on a four-year brand. That

5 would be --

6 A No, no.

7 Q I'm sorry.

8 A If I did not make myself clear, I think I said --

9 THE COURT: I understood. Go ahead.

10 MR. ODELL: You were going to correct me?

11 THE COURT: No, he was going to repeat himself

12 on an explanation he had already given.

13 Let's go forward with your questions.

14 Q Now, there are some whiskeys sold by Schenley

15 that don't have to be aged at all, is that correct?

16 A Yes.

17 THE COURT: What is distilled? I don't know

18 anything about it.

19 THE WITNESS: Distilling, sir, is the process

20 primarily of taking a grain or a cereal-like corn and mashing

21 it, adding yeast to it, letting it ferment for a number of

22 days, 72 to 96 hours.

23 Then you let the mash run off, so to speak, and

24 you take the fermented portion and put it into a still where

25 you bring it up to a tremendous steam posture. You, in

effect, convert that liquid into steam.

In the process, depending upon which proof you distill at -- and there are technical aspects there -- in the process, you create vapor and when that vapor condenses, you have the new distillate, raw, fresh off the still.

THE COURT: It is to that which you add the alcohol?

THE WITNESS: No, the alcohol starts to come in in the process of fermentation and then in the distillation process right in the still.

THE COURT: Thank you.

MR. ODELL: Judge, you need a license to be a distiller.

THE WITNESS: You do.

BY MR. ODELL:

Q I just wanted to ask you a couple more questions about this process of planning production for needs four years ahead if it is a four-year brand or six-year brand.

You have to have some margin of safety in your prediction to the extent it is based on current sales and I believe you have explained that there is such a margin and it is generally a margin in favor of having more whiskey there if you can sell it rather than not having it, is that

correct?

A That would be preferable generally.

Q Is it a disastrous mistake in terms of money if, for example, you produced 100,000 more cases of bourbon or barrels of bourbon in a given year? What is the content cost of a barrel of bourbon?

A Which is your question?

Q What is the content cost of a barrel of bourbon?

A That would depend as a function of the price of grain and the price of fuel in order to distill that.

Q We understand that, but is there a rule of thumb price based on Schenley's experience as to what the content cost alone is of filling a barrel in the first year of production of a bourbon?

MR. SILVERMAN: Is there any year you want to do this in?

Q Let's say 1968.

A Well, there are significant differences in years depending upon the price that you must pay for the corn, and as an agricultural product, that is not static, and the price you must pay for fuel which, as you know, can run all over the map depending upon whether you use oil, coal or gas.

But to be very specific, at one point in time when corn was at a dollar a bushel, the content, not including the

barrel, would have cost you approximately fifty to sixty cents an original proof gallon.

Q And how many gallons in a barrel?

A The liquid content of the barrel is designated as 50 gallons. However, since you are putting it in at a proof higher than 100 proof, you generally have 65 original proof gallons laid away in each barrel.

Q You said that price was about what? I didn't quite catch it.

A Fifty to sixty cents, again depending upon what it cost you at that point in time for grain and other --

Q And just to fill out --

A That is, not including the barrel, though.

Q I understand, just the content cost we are talking about.

An original proof gallon is a gallon that is 100 proof, is that correct?

A It is one liquid gallon at date of distillation at 100 proof.

Q So that if the whiskey in that barrel is being made for an 86 percent or 86 proof whiskey, at the time the barrel is dumped for bottling, some water is added to reduce the proof to 86 percent, is that correct?

A At the time of bottling.

2 Q To the extent there is that shrinkage from
3 100 proof to 86 percent, the cost goes down by proportion,
4 is that correct?
5 A Yes.
6 Q The other question I wanted to ask you was,
7 are you familiar with the standards by which other distilling
8 companies like, say, National Distillers, whether their
9 method of planning new production is similar or different
10 than yours? Are you familiar with their method?
11 A I have no direct knowledge. Just a presumption
12 that it quite logically would have to be similar.
13 Q I started the question. I don't know whether I
14 got the answer.
15 I wanted to have you explain briefly those
16 whiskeys that did not require aging for purpose of sale in
17 bottles.
18 A The distilled spirits, to be more precise in
19 terminology, that don't require aging are gin and vodka.
20 Q And those distilled spirits that go into gin
21 and vodka are manufactured from time to time by Schenley, is
22 that ocrrect, in its various distilleries?
23 A They are.
24 Q What is the cost per gallon of distilling of a
25 neutral grain spirit?

2 A At what point in time?

3 Q At 1970, sir.

4 A 1970? The approximate cost to product a proof

5 gallon of grain neutral spirits was, give or take, 35 cents.

6 Q I wanted to give the Court an idea here of the

7 particular areas of concentration that Schenley had in the

8 whiskey business in terms of straight whiskeys, Scotches,

9 Canadians and so forth and before I show you this chart,

10 just let me ask you one or two more questions.

11 Straight whiskeys, like bourbons, have to be, at

12 the time of distillation, have to be stored in new barrels,

13 is that correct?

14 A To be designated as bourbon whiskey, it has to be

15 stored in a new barrel.

16 Q Is that similarly true of Tennessee whiskey?

17 A Yes.

18 Q Tell me whether Canadian whiskeys, that is to

19 say, whiskeys labeled Canadian, generally made in Canada,

20 whether those whiskeys can be made with new or old barrels.

21 A They can be made with either but they are, to the

22 extent of about 99 percent, made -- produced with and stored

23 in used cooperage.

24 Q And that is because the cost of used cooperage

25 is substantially less, is it not, than new cooperage?

A There is no question the cost is substantially less but it is a historical fact and I don't know what originated the raison d'etre for used cooperage in Canada.

THE COURT: When you come to a convenient stopping point, you tell me.

MR. ODELL: I can't stop when we are talking about whiskey, your Honor.

Just let me finish with this little area.

Q Let me show you Plaintiffs' Ex hibit 44 for identification, schedule that was prepared and given to me by the Schenley people.

(Counsel conferring.)

MR. SILVERMAN: We have no objection.

MR. LEVIN: No objection.

MR. ODELL: May it be offerered, your Honor.

THE COURT: Received.

(Plaintiffs' Exhibit 44 for identification received in evidence.)

MR. ODELL: May I also offer 43 for identification to which the defendants have no objection.

THE COURT: It may be received.

(Plaintiffs' Exhibit 43 for identification received in evidence.)

MR. ODELL: Your Honor, I think the time has

1 come.

2 THE COURT: We will recess until ten minutes

3 after two.

4 (Luncheon recess.)

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AFTERNOON SESSION

2:15 p.m.

(In open court)

THE COURT: Before we start, I want to apologize for being a couple of minutes late, but the best analogy is if you light a fire under a pot, it will eventually boil.

I have considered the law on whether or not fairness as a pendant claim is properly before me. I have concluded, in my discretion, that it is not. I may be persuaded to the contrary, should you prevail on the disclosure claims, but I will leave that open. But, in any event, given the history of this case, I read Judge Lasker's ruling and I note that he even makes it as an assumption that federal jurisdiction has been properly invoked on the fairness claim, and I read the opinion of Chancellor Marvel, who makes a finding that the -- in totality of the opinion as I see it, he makes a finding that the burden being on the defendants to establish fiarness within the control that they had, he finds that fairness has been established.

Am I right about that, Mr. Silverman, in the overall --

MR. SILVERMAN: Yes, sir. After a very full

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record.

THE COURT: I also note that these cases are one day apart. Judge Lasker comes down on one day and Chancellor Marvel comes down on the next.

Given that and other factors which we have discussed this morning, and I don't really mean to relate them again, it seems to me fairness has been the subject of an action in the proper forum in a fully litigated manner, and as I read Mine Workers v. Gibbs, 383 U.S. 715 at 725 and 726, it's crystal clear that pendant jurisdiction is a matter of the Court's discretion. It is not a matter of the plaintiffs' right. It does not depend on whether or not federal claims are dismissed before trial or whether you ride into trial with the pendant jurisdiction before the Court acts.

It specifically points out the need to avoid conflict with a state court situation as a matter of committee, if that should appear, and it certainly, in my judgment, does appear here.

As a consequence, I am going to rule that to the extent that evidence has been offered before me on the issue of fairness alone, I would exclude it. To the extent that it's being offered on the issue of failure to disclose something, I will receive it. We will go forward on that

3 lzmch

basis.

MR. ODELL: Your Honor, I'm not going to argue this any more. I would just like to ask you that, while I think I'm going to prevail on the defects in disclosure here, I would like to be able to be heard on this question that you have just ruled on because I really have submitted no authorities and I have given you the arguments off the top of my head, and more important than anything else is that these same kind of arguments were urged before Judge Weinfeld in knocking out this case as a class action, and he just ignored it, but more important than that, your Honor, rulings and holdings on applications for temporary injunctions, unless you have a full hearing and a final injunction, are not considered res judicata or collateral estoppel.

There is lots of authority on that. If I had the time to go into my files, those points were raised before Judge Weinfeld. I'd like to at least have the opportunity to be heard on that a little later in this case and let me go on with this witness.

THE COURT: I will permit you to come before me again with this issue, but your posture at that point is going to be in the nature of reargument. I'm not going to keep the issue open.

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MR. ODELL: But, your Honor, I haven't argued it. I don't want to start a difference with you about that.

THE COURT: I'm sure you had Mr. Silverman's brief --

MR. ODELL: No, we didn't. We only had his damage brief, his brief as it relates to damages.

THE COURT: You were certainly aware of the fact that these decisions had been rendered in this court and in Delaware.

MR. ODELL: I was aware of them before Judge Weinfeld when I thought they were disposed of and ruled on.

THE COURT: Judge Weinfeld, in ruling on class action, does not bind me on the question of pendant jurisdiction.

MR. ODELL: I agree with that, sir.

THE COURT: Fine judge that he is.

MR. ODELL: All I am saying is that I don't -- I think the law is clear that a ruling on a decision on applications for temporary injunctions is not dispositive of the issues.

THE COURT: Just to make it perfectly clear, I'm not relying on that. I am relying on that in part, but in further part on the fact that there has been a hearing on value in Delaware, which is now on appeal, and the

5 lzmch

difference between the $29 and the $30-something is not, in my judgment, such as to raise a question of fairness. It is to raise a difference of opinion as to value, which is what Chancellor Marvel points out.

He says that if it's only a dispute in value of the stock, then an appraisal is sufficient. I haven't heard anything to the contrary.

Let's go forward. You have my position. I have ruled on it and I'll give you the opportunity to come back to me.

MR. ODELL: I am perfectly content to deal with this as a matter of reargument, but please bear in mind that I should not be confined to the ten days within which to ~~appeal~~ reargue.

THE COURT: I would not confine you to that as a matter of law. I am just saying I want you to be aware there is now a ruling in the case, and the parties are going to go forward on the basis that there is a ruling in the case, so that -- because this represents my best judgment.

I am prepared to hear you to see if you can change that, but that represents my best judgment, and having reached that I am prepared to go forward on that basis.

MR. ODELL: I won't say okay, your Honor --

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THE COURT: I understand that you don't.

MR. ODELL: Your Honor, may I have your permission to be seated while I am asking the questions?

THE COURT: Sure, go right ahead.

MR. ODELL: May I say, before I get into these two exhibits which were admitted that I didn't get into, that in my examination of Mr. Chernow I have intentionally eliminated a good many of the questions that deal with testimony that he gave in his deposition, and I'm working on the assumption, and I ought to be corrected immediately by my adversaries and certainly make it clear to you that in their effort to expedite this, the interrogation of these witnesses, I would like the full deposition of Mr. Chernow to be admitted in evidence here and to be before the Court, and I will -- as the Court will see, I will limit myself to almost the barest references to his previous testimony in the deposition.

MR. SILVERMAN: If your Honor please, as I understand it, the pretrial order required Mr. Odell to inform us of what portions of Mr. Chernow's deposition he would rely on and,if he intends to go beyond what he has informed us of, I will consider it inappropriate.

MR. LEVIN: If your Honor please, I think Mr. Odell has to elect as between calling the witness and then

7 lzmch

making some arrangement with respect to his deposition.

THE COURT: I'm not so sure I will go further with it in the interest of time, but, certainly, matters that have been brought out in an earlier fashion that can be gotten before me quickly and summarily and are not a subject of dispute, but I do think if you are going to rely on certain parts of the deposition, that the other side ought to be informed, because there may be parts of the deposition that are hearsay or speculation or otherwise objectionable to one side or another.

It would seem to me not inappropriate that you or Mr. Zulack just take a red pencil and block off the places you want and show them to the other side.

MR. MANNING: It's also important we know what portions of the deposition he relies on so we can frame any cross-examination we might want. We don't know what's going on. We don't know what to cross-examine about.

MR. ODELL: I have already mentioned some portions. I assume these are in addition to that.

D A V I D A. C H E R N O W, resumed.

MR. ODELL: Your Honor, one of my purposes in offering these exhibits, No. 43 and 44 in evidence, particularly 44, is to show the types and relative amounts of the different types of whiskey that have been sold by

Schenley from 1966 to 1971. This is really to give your Honor a quick glimpse of how the total sales of cases and bulk whiskey have increased by Schenley, and then, after these exhibits, I will get to the dollars. These only talk in terms of cases and they relate to an exhibit in the proxy statement that speaks in terms of percentages rather than numbers of cases sold.

The reason for percentages, rather than numbers, I understand, is that those are case sales, and are considered a very confidential thing among competitors in this business so, with your permission, I would like to show you this Exhibit 44 for that purpose.

I also show one to Mr. Chernow if he would like to see it.

44 in the very last column shows the sales, excluding Buckingham, for 1970.

Now, your Honor, I would like to get to the dollars, and dollars get expressed in various financial statements prepared by Schenley. First, I'd like to offer in evidence the Schenley annual report sent to its stockholders for the fiscal year ending August 31, 1968, Exhibit 7.

THE COURT: Let me ask you this: Are you going to lay this foundation and ask this gentleman questions based upon these exhibits?

9 lzmch Chernow-

MR. ODELL: I don't intend to ask him any questions because I think the exhibits speak for themselves.

THE COURT: Why don't I hold the exhibits until you are through with his testimonial interrogation, rather than have him sit here while we just put exhibits on?

MR. ODELL: It seems to me if there is going to be any objections raised by the defendants that this witness can answer and perhaps qualify the exhibits for admission, that it would have to be done in his presence. That was the whole thought of trying to get these cleared in the absence of him and before he went on the stand.

THE COURT: They don't question these exhibits.

MR. ODELL: They don't question the authenticity of these exhibits. Their only objection to them is relevancy.

Am I correct?

MR. SILVERMAN: I don't know which exhibits you are now talking about.

THE COURT: 43 and 44.

MR. ODELL: Those have been offered. I'm through with those.

I am now going to the financial statements which will begin with Exhibit 7, the annual report of Schenley for the year ended August 31, '68. I thought your question

was addressed to that.

MR. SILVERMAN: Again in an effort to be helpful, if Mr. Odell will go forward with Mr. Chernow on the testimonial part of his case, we will guarantee that if there are any questions at the time that the exhibits are offered and if Mr. Odell feels --

THE COURT: He doesn't want to inquire. He wants him here in order that you may inquire.

MR. SILVERMAN: We may inquire?

THE COURT: Yes.

Is that right?

MR. ODELL: My understanding is there is no objection to these exhibits except relevancy. They tell several stories in the language and words of the defendants.

THE COURT: Let's start with a fresh record, please.

Can we question this gentleman until everybody is finished with him and then let him go? Can we do that?

MR. ODELL: All right, let me try.

THE COURT: Let's do that.

DIRECT EXAMINATION CONTINUED

BY MR. ODELL:

Q Mr. Chernow, are you familiar with the fact that for the year ended August 31, 1968 Schenley's income was

some -- net income after taxes was some $4,300,000 less than it was for the fiscal year ended August 31, 1967?

THE COURT: Read that question back, will you please.

(Question read)

A If you will show me a copy of our annual report I can refresh myself on the specifics.

(Document handed to the witness)

A I don't read it that way.

Q Well, how do you read it?

A According to our financial statement, the net income for the year ended August 31, 1967 was $22,726,000. The net income for the year ended August 31, 1968 was $16,794,000, approximately $6 million difference.

Q To what was that decline due?

A Excuse me. I didn't hear you.

Q To what factors was that decline from '67 due?

A It was due to quite a number of factors, part and parcel of the course of ordinary operations of the business, as well as the failure to have a gain on a disposition of real estate and certain year-end adjustments in August of 1968.

Q And were those adjustments the ones that are referred to on the first page of this annual report as

being income tax surcharges, higher interest costs and other transitional costs relating to marketing and organizational changes?

A Essentially, yes.

Q Looking at that income statement again for just one moment, Mr. Chernow -- looking at that income statement for one moment, I notice that for the year ended August 31, 1968 Schenley's selling, administrative and advertising expenses increased by about $11 million to $75,907,000 from $64,775,000.

Do you notice that?

A I read it.

Q I'm going to ask you to look at Exhibit 14 for identification, which is the statement of Schenley before audit reclassification for the year ended December 31, 1969, and which compares the Schenley earnings for the calendar year December 31, 1969 with those for the calendar year 1968, and ask, after you see this exhibit, whether the details that are shown on that comparative income statement of Exhibit 14 for identification set forth the details of increases in expenses for the calendar year 1969 over those for the calendar year 1968?

A It does.

MR. ODELL: Your Honor, off the record for just

one minute.

(Discussion off the record)

THE COURT: We are now on the record.

MR. ODELL: I offer Plaintiffs' Exhibit 14 for identification.

THE COURT: Any objection?

MR. SILVERMAN: No, sir.

THE COURT: Received.

MR. ODELL: I also offer Exhibit 7 for identification, which is the annual report for the year ended August 31, 1968.

MR. SILVERMAN: Offered for these purposes, we have no objection.

THE COURT: Received.

Plaintiffs' Exhibits Nos. 7 and 14 were received in evidence.)

Q I would also like you to look at Plaintiffs' Exhibit 7 for identification on the first page where the following sentence appears --

THE COURT: 7 is in evidence now.

Q -- "We have set future plans so the company will become even more dynamic and successful."

I ask you what those plans were.

A Fundamentally, to maximize the sales of our

profitable brands. When you cull it all down, that is the thrust of what makes a distiller a profitable distiller, when you can sell more cases of your more profitable brands.

Q Increased sales of more profitable brands of whiskeys manufactured or distributed by Schenley, is that what we are talking about?

A Essentially, correct.

Q In the calendar year 1969, did some of those plans referred to as future plans in 1968, did they bear fruit in 1969?

A Some of the brands certainly did increase in volume. I don't have the specific recollection here at this point.

Q Is that reflected in the annual report of Schenley for the calendar year December 31, 1969? The fruition of the plans to increase or maximize the profits discussed in '68.

A Every function of the company as it relates to either greater or lesser profits gets distilled down to the bottom line of the company.

Q Mr. Chernow, both you and I are having voice troubles. I think all you have to do is to say "yes" to that question.

MR. SILVERMAN: Objection to that comment, your

Honor.

THE COURT: Sustained.

Q I show you Plaintiffs' Exhibit 8 for identification, the annual report of Schenley, and I'd like to ask you some questions about it.

A For what year are you referring to? This looks like Fed 1-A --

THE COURT: Is this the Schenley report for 1969?

MR. ODELL: Yes.

MR. ZULACK: It's a different marking. It's the same exhibit.

THE COURT: You both have the same exhibit. What is the question?

MR. ODELL: I asked him to look at the first page.

Q Look at the first paragraph on the first page. Your management is proud to report sales of $643 million, the highest in two decades, and the second highest for Schenley's all-time net income of $25.3 million in earnings per common share of $2.78.

Is that a true statement in terms of the reference to the sales being the highest in two decades?

A It is a true statement as it is reflected here

in the letter to the shareholders.

Is the second paragraph which speaks about increases in case sales by over 2 million cases a true statement as it appears there?

A It is a true statement.

Q Look at the very last paragraph which reads, "Schenley's exciting record in 1969 not only moved the company stirringly ahead but also provides a springboard for greater advances in the future. Subject to the vagaries of national economic factors that we cannot foresee or control, your management anticipates continued gains in Schenley's share of the markets it serves."

Is that an accurate statement of what it purports to say there?

A I don't know what your reference is of what it purports to say.

Q I'm sorry. That was an inept question and I apologize.

Did you, as a director of Schenley, concur in the hope and expectation that is expressed in that last paragraph?

A I am very optimistic about increasing Schenley's market share.

Q The question is, were you in 1969?

A I was then; I am now.

Q You were then and you are now; very good.

MR. ODELL: I offer in evidence Plaintiffs' Exhibit 8 for identification.

THE COURT: Any objection?

MR. SILVERMAN: No objection, your Honor.

THE COURT: Received.

(Plaintiffs' Exhibit No. 8 was received in evidence.)

Q Did Schenley's sales continue to increase and did its profits continue to increase in 1970?

A My best recollection is that they did, although I don't have the figures in front of me to be specific.

Q I show you the annual report for the calendar year 1970, which is Plaintiffs' Exhibit 9 for identification.

You have the report in front of you, Mr. Chernow?

A Yes, I do.

Q I ask you to look on the first page at the first paragraph.

THE COURT: Mr. Odell, are you going to do more than just identify the exhibit?

MR. ODELL: I'm going to ask him a few questions, just the way I have on the previous ones.

THE COURT: All right.

Q Could you tell me, first, when was this opinion distributed to the stockholders of Schenley?

MR. SILVERMAN: This what?

Q This annual report distributed to the stockholders of Schenley.

A I couldn't give you a specific date in time, but I would have to resume that it would be sometime towards the end of March of 1971, or possibly sometime the beginning of April.

Q Would you look at the first page and the first paragraph of that annual report?

The first sentence reads: "Schenley continued to make progress in 1970."

In the position that you held as an officer and director of Schenley in 1970, is that first sentence an accurate statement?

A Is it an accurate statement?

Q Statement.

A Yes.

Q Now, just read on another sentence or two which reads as follows:

"The brands that were heavily supported were carefully limited to a comparatively small number with either proven profitability or promising future potential."

Would you please tell me what brands were those that had "proven profitability," and what brands had "promising future potential," as referred to in this annual report of 1970?

MR. SILVERMAN: If your Honor please, I rise now, having desisted up until now.

I do not understand this line of questioning in light of your Honor's ruling, unless my friend intends to link it up with some failure to disclose a disclosable fact in the proxy statement. If he represents that he will -- that this is part of his failure to disclose, rather than to show fairness or whatever, I will obviously withdraw my objection, but I think that until now we have a series of questions which I think perhaps ought now to be tied into this case.

MR. ODELL: May I answer that?

THE COURT: Please do.

MR. ODELL: First, your Honor, there has been some objection regarding the admissibility of any records after the date of this merger, and it's been my position, and I will cite cases to your Honor to support the proposition, that events that were operative prior to the date of the merger --

THE COURT: No, we are not talking about the

use of materials before or after to establish a fact. I agree with you on that.

The question here was to what alleged failure to disclose is this area of inquiry addressed? That's all Mr. Silverman is asking.

MR. ODELL: Your Honor, it does not, strictly speaking, go to the question of nondisclosure. It does go to the question of damages.

THE COURT: Then I sustain the objection.

MR. SILVERMAN: If your Honor please, I move to strike this line. However, if my friend wants to offer the annual report, I have no objection to its being admitted.

(Continued on next page)

MR. ODELL: Your Honor, may I finish?

One of the other -- one of the defects in disclosure that we claimed here was that the opinion of Allen & Co. that's found in this prospectus is to the effect that the terms of this merger were fair and equitable. I will show in the course of my examination of Mr. Chernow a little later that one of the bases for Mr. Shuman, the Vice President of Allen, who gave that opinion, that Schenley's stock was worth what he said it was worth was that Schenley had an unimpressive growth record. And he referred to sales figures, some case sales, what he called deplation figures. And these annual reports and some others in this line and financial information that I propose to offer through Mr. Chernow and one more witness, we will show that had Mr. Shuman been told the truth or, put it another way, had Mr. Shuman told these directors who hired him to pass on this merger as being fair and equitable, had he told them the reasons that he gave in this affidavit opinion of his for downgrading the value of Schenley, as he did, then these directors were misinformed or accepted an opinion that they knew was wrong.

THE COURT: Let's go ahead. If it is your intention to show that Allen & Co. was given misinformation and this is to prove that fact --

MR. ODELL: Right. It is a little broader than

that. I don't want to give you the outer limits of what I am trying to prove.

THE COURT: Isn't that enough to make it admissible at this point.

MR. ODELL: It certainly is in my opinion. I am trying to say that's not the whole of my point and it will develop as we go along.

MR. SILVERMAN: Do I understand it is Mr. Odell's contention that Allen & Co. was not furnished with this information?

THE COURT: No. This is the information that he contends is to the contrary of what Allen & Co. was furnished, therefore rendering Allen & Co.'s opinion conspiratorially misleading. Is that right, Mr. Odell?

MR. ODELL: Your Honor said it better than I could.

MR. SILVERMAN: That's a very big word, your Honor.

THE COURT: That is what he is saying. I will admit the evidence for that purpose and we will see whether it measures up to what he offers it for.

MR. ODELL: I think we had a question that was not answered and interrupted by an objection. What was the last question, Mr. Reporter.

(Question read.)

THE COURT: Can you answer that?

A Yes. Without being in a position to detail each and every one, there certainly were some brands that can be identified. For example, Dewars White Label. Another example, Dubonnet Aperitif. Another example, George Dickel. Each in its own position. Each in its own size frame.

Q May I add another one, Mr. Chernow, with your permission, the Mateus brand of wines?

A Be my guest.

Q The next sentence reads, "Eight categories of products were accorded major attention. Scotch --" and you have referred to Dewars I take it in Scotch. You referred to Bourbon. What were the brands in Bourbon?

A Old Charter. I.W. Harper. Ancient Age.

Q I am not trying to trap you by limiting to you what you say. In due course we will get to the figures that show the brand sales by year. I would just like to go on.

Did the Schenley case sales and profits increase in the calendar year 1971?

MR. SILVERMAN: 1971?

MR. ODELL: Yes.

A Well, you have to -- if I can be permitted to see the report.

MR. ODELL: Your Honor, can I offer 9-D in evidence -- 9 for identification in evidence. I offer it in evidence.

THE COURT: The '72 report?

THE WITNESS: The '71 report.

(Plaintiffs' Exhibit 9 received in evidence.)

xx

A As it relates to sales --

Q Have you got the report?

A Yes.

Q You are looking now at Exhibit 10; is that correct?

A Exhibit 10. As it relates to sales, they did increase in the year 1971 -- December 31, 1971. As it relates to income before extraordinary items, they decreased from the prior year.

After extraordinary items are included, net income increased as against the prior year.

Q As long as you are on that page I think we ought to eliminate any possible confusion as to what you just said. One reason for the decrease was the sale of Buckingham, is that correct, in 1971, decrease in earnings that you referred to?

A Yes.

Q And if you look at that annual report, there is a line there that reads, "Income from continuing operations."

A Yes.

Q Now, that line excludes income from Buckingham for '70 and '71; is that correct?

A That income from Buckingham is separately detailed as you see.

Q So there is no confusion about this as we go along, the profits from continuing operations are increased from 18,473,000 in 1970 to 22,289,000 in 1971. There is no doubt of that, is there, after you have seen the annual report?

A There is no doubt about it.

MR. ODELL: I offer the annual report for the year ended December 31, 1971.

MR. SILVERMAN: I have no objection.

xx (Plaintiffs' Exhibit 10 received in evidence.)

Q Did the factors that were at work in 1970 and 1971, the factors that would work in Schenley that were increasing its sales and its profits, did they continue into 1972?

MR. LEVIN: I object, if your Honor please.

MR. SILVERMAN: Objection.

THE COURT: Yes, how is that relevant?

MR. ODELL: Your Honor, it is relevant, first, to show and again I'm going to have to refer to Mr. Shuman -- first let me say that Mr. Shuman is referred to in this proxy statement at page 5, paragraph numbered 9. The investment

2 banking firm of Allen & Co. has acted as advisor to the Board
3 of Directors of Schenley in connection with the proposed
4 reorganization and has advised the Board that in their
5 opinion the terms of the proposed reorganization are fair and
6 equitable to the holders of Schenley common stock and $1.40
7 preferred stock. I'm not trying to emphasize that paragraph.
8 There is more in that paragraph and I think your Honor has a
9 copy of that proxy statement. Mr. Silverman, I believe,
10 gave it to you. It goes on and talks about rendering its
11 opinion and I am going to paraphrase this in the interests
12 of --

13 THE COURT: The question is, how does this last
14 question to which there is objection, how does that --

15 MR. ODELL: I will get to that, your Honor.

16 One of the elements -- Mr. Shuman's opinion, his
17 written opinion that we have here -- one of the parts of his
18 opinion reads --

19 MR. SILVERMAN: What opinion are we talking about?

20 MR. ODELL: We are talking about the affidavit
21 of Stanley Shuman that was filed in the Green action, and as
22 far as I know it is the only writing extant that specifies
23 the grounds for the opinion given orally to the Board of
24 Directors of this company, as I will show later, at a
25 director's meeting prior to the effective date of the merger.

THE COURT: How does that tie in with this last question?

MR. ODELL: Your Honor, I am going -- I am not a lefthanded pitcher but a long winder.

One of the statements in this affidavit of Mr. Shuman's is "I do not believe it reasonable to conclude that Schenley's past growth rate will markedly improve in the future. That's his opinion as of June 7, 1971. And the purpose of introducing the '72 reports, just like the same purpose of introducing the '71, is to show that the seeds were planted with the expectation that they were going to bare fruit and the fruit was borne. And that expectation of profit, as shown by the statements prior to the merger, properly speaking with a fair subject of an opinion -- a fair subject and certainly relevant to any opinion expressing the value of the stock. The earnings potential of a company is an important factor in determining the value of the stock and whether the merger is fair and equitable.

THE COURT: You are talking now about a time that is after the merger.

MR. ODELL: I am, your Honor, and there is no question about it.

THE COURT: How can that bear upon what representations were made at the time of the merger? That is what your

2 objections were based on, is that so?

3 MR. LEVIN: That is correct.

4 MR. ODELL: Your Honor, first I pointed to some
5 cases in this district where the Courts went as much as two
6 years after the date of the merger or the sale of assets and
7 said the purpose of going forward is to test the accuracy of
8 the suppositions and to prove the continuation of facts that
9 were operative at the time of the merger that related to the
10 value of the stock for the purpose of merger.

11 THE COURT: That makes some sense. What about
12 that, Mr. Levin?

13 MR. LEVIN: If your Honor please, this entire
14 line is being admitted upon the proposition and upon the
15 representation that somehow or other it is going to be
16 connected with a conspiracy in which either Shuman was involved
17 or not involved but, in any event, the Board of Directors was
18 involved, so that Mr. Shuman would be deceived or would in
19 complicity with us render a phony opinion which would be put
20 in the proxy statement. That's the representation. This
21 doesn't shed -- this is absolutely without probity on that
22 issue. Would Mr. Odell suggest that these annual reports,
23 with the statements that he is reading with such elaboration
24 into the record, were not given to Mr. Shuman? Clearly he is
25 not going to make that representation to your Honor.

2 THE COURT: That statement to me which I am
3 addressing myself to is that some financial data in the merger
4 proposal showing a state of mind on the part of condemned
5 management can be put in substantial doubt by events that
6 followed within the two subsequent years. That is what his
7 last statement to me was. Am I right?
8 MR. ODELL: That's right, sir.
9 THE COURT: It seems to me on that basis --
10 MR. SILVERMAN: Your Honor, I would ask you to also
11 include in that formulation, because it is necessary to my
12 friend's conduct, that it isn't only management but that
13 somehow management and/or Shuman with an evil intent --
14 THE COURT: All I am doing at this point, Mr.
15 Silverman, is receiving evidence. Whether it has any weight,
16 whether there is any -- some fact to which he will be able
17 to address -- connect up with the subsequent facts, I am not
18 prepared to say.
19 MR. SILVERMAN: Your Honor has ruled. I will
20 sit.
21 THE COURT: I will accept it. The last question
22 had to do with what was his belief about the future fortunes
23 of Schenley at a particular time; is that correct? That was
24 the last question?
25 MR. ODELL: What was the last question, Mr.

2 Reporter?

3 (Question read.)

4 THE COURT: Can you answer that question?

5 A It is a bit vague but I would say that, again,

6 subject to confirmation by the numbers those factors were at

7 work in our efforts to increase sales and profits.

8 Net sales for the year ending December 31, 1972

9 were 693 million against 637 the prior year with income

10 before extraordinary items, 26,646,000 against 25,012,000 the

11 prior year.

12 MR. ODELL: Your Honor, I offer Exhibit 11 for

13 identification in evidence.

14 MR. SILVERMAN: No objection.

15 THE COURT: Received.

xx 16 (Plaintiffs' Exhibit 11 received in evidence.)

17 Q One more thing I would like to go into with you

18 on 11 in evidence. The very last page of Exhibit 11 compares,

19 shows on a comparable basis Schenley's income from continuing

20 operations from August 31, 1968 to December 31, 1972 and

21 those being the last five-year earnings of Schenley prior to

22 December 31, 1972. For comparative purposes and based on

23 your knowledge of the business and affairs of Schenley,

24 would you say it was fair in measuring the sales, progress

25 and increases in income of Schenley to compare the year ended

2 August 31, 1968, say, with December 31, 1971?

3 MR. SILVERMAN: Objection, your Honor. I don't

4 understand the relevance.

5 THE COURT: I don't understand.

6 MR. ODELL: May I explain it?

7 THE COURT: Please do.

8 MR. ODELL: The witness testified earlier with

9 respect to an exhibit that compared the 1968 earnings to the

10 1969 earnings, that in 1968 there were some transitional

11 costs that were responsible for the earnings for the year

12 ended August 31, 1968 being less than those of the preceding

13 year, August '67 and for want of a better word, your Honor,

14 I would like to say that those transitional costs were

15 incident to the new management of Schenley taking over.

16 Q Is that a fair statement, Mr. Chernow?

17 A They were coincident, yes.

18 Q Thank you very much.

19 And can expenses of the kind that are non-

20 recurring and taken once --

21 MR. ODELL: I am trying to get from this witness,

22 who I have found to be a fair and reliable witness, I must

23 say --

24 THE WITNESS: Thank you.

25 MR. ODELL: -- and one that's been very frank with

me in the course of his depositions, I might add, I am trying to find out from this witness whether it is fair to compare an increase of earnings --

THE COURT: The only quarrel your adversary has with you is the use of the word "compare." If you want to establish there are factors in there that are non-recurring that permit me as the trier of the fact to determine that you cannot fairly compare those years, that I will permit you to do.

MR. ODELL: That is all I was trying to do.

THE COURT: Why don't you do it on that basis and go after what the facts are.

MR. ODELL: I believe he testified already to what facts there were that reduced those earnings.

THE COURT: All right.

Q In a comparison of Schenley's earnings for the years 1971, for example, would the year ended August 31, 1967 be a more typical year to reflect the operations of Schenley than the year August 31, '68?

A I don't think any single year can be identified as a typical year. Each year has different problems that are resolved as they go along and there is no single cold standard against which you can measure any other year.

Q Well, Mr. Chernow, may I borrow on your knowledge

and experience in the financial community. Comparisons are made in the financial community of earnings of a company from year to year; is that correct?

A There are comparisons from last year or over a period of years, yes.

Q You start with a base and depending on where you want to end up, you make that comparison; is that correct?

A It depends upon what the purpose of your comparison is intended to do.

Q The purpose of my comparison here is to determine from you whether for the purposes of measuring the growth in Schenley's sales and income for the years that began under the new management, and I believe that first year would have been December 31, 1969; is that correct?

A If you are talking about a full total twelve months incorporated within a fiscal year, I would have to agree that's the period.

Q I want to get from you your judgment as to -- if I were to compare calendar 1969 with calendar -- with fiscal year August 31, 1967, would that be a more representative and typical measurement of the progress and extent of the improvements in earnings brought about by this new management than if I used the year August 31, '68?

MR. SILVERMAN: Objection.

MR. LEVIN: Objection.

THE COURT: Sustained as to form. This doesn't get a helpful answer to me. The word "more typical," what do I conclude from that? That is the problem.

MR. ODELL: What I am getting at is that because of the non-recurring expenses reflected in the year August 31, 1968, which reduce the earnings -- I am arguing against myself here. I might tell you that. Because if I were trying to show --

THE COURT: This gentleman has said no year is typical. That you have problems every year and you solve them. Am I correct in that?

THE WITNESS: Yes, sir. You attempt to solve them.

Q What were the problems for the year ended August 31, 1968?

A Pardon me?

Q What were the problems that you had to solve in the fiscal year August 31, 1968?

MR. LEVIN: Can that be related to something, your Honor. There must have been a multitude of problems that are irrelevant.

MR. ODELL: I am using the witness' words. He said "problems."

2 THE COURT: Well, you are trying to make a showing
3 of the trend of the company, is that what it amounts to?
4 MR. ODELL: Your Honor, it is getting late and
5 I don't want to make -- I don't want to extend this any more.
6 Mr. Shuman in his evaluation of this company in his affidavit
7 compared the earnings of Schenley for the calendar year
8 August 31, 1968 to the calendar year December 31, 1970, and
9 he said that the increases that are shown here --
10 THE COURT: Is he going to be here?
11 MR. ODELL: I've got him subpoenaed, your Honor.
12 I was hopeful that with Mr. Chernow's testimony, it might not
13 be necessary to bring him. It is not the easy way to do it,
14 I might state, but I think it might be quicker.
15 What I am trying to say is, Mr. Shuman said, and
16 I'm going to -- he said the increase to $18,473,000 at
17 December 31 -- for the year ended December 31, 1970, as
18 compared to the $11,826,000 at August 31, 1968, was due to
19 two things, neither one of which had very much to do with
20 Schenley's sales or increased income.
21 First he said there was a cost reduction program
22 and second, he talked about these transitional costs which
23 brought down Schenley's income in August of '68 by the sum
24 of some $7 million which Mr. Chernow testified about earlier
25 and he said that between those transitional costs and the

2 cost reduction program that he said, whose full impact was
3 not felt until 1970, there was no real improvement of
4 Schenley's earnings between those years.
5 I will show you subject to connection, of course,
6 I will show you that this cost reduction program, its full
7 impact was felt in 1969 and not in 1970.
8 THE COURT: Is that what you are trying to ask
9 this gentleman?
10 MR. ODELL: No, I haven't gotten to that yet.
11 I'm trying to get to the fact that to make this comparison
12 between '68 and '71, as Shuman did, to indicate a lack of
13 growth and a lack of improvement in sales and earnings and to
14 blame it on these two factors, transitional costs and
15 reduction in -- the cost reduction program is in part not
16 true and in part it is not a fair comparison to make for
17 purposes of appraising value and that the comparison, if
18 anything should have been made between December 31, '69 and
19 '70, in August 31, '67, where you did not have these
20 transitional costs which reduced earnings in '68 --
21 THE COURT: Is it inappropriate for me to suggest
22 that you take the factors of Mr. Shuman's with which you
23 quarrel and assign them to a particular time period and then
24 ask Mr. Chernow what his recollection is of those factors in
25 that period.

MR. ODELL: Your Honor, I have to apologize to you. I thought this was something that was not to be disputed or to be misunderstood by Mr. Chernow. I told you how I felt about him before.

MR. LEVIN: Your Honor, I would be helpful if I understood what was going on. That's my problem.

MR. ODELL: Abe, the problem is you have not done your homework.

15/75 end

THE COURT: We will take a fifteen-minute recess at this point.

Before we do, incidentally, what causes of action are presently before me from this complaint?

Number one, the number two cause of action is now out.

MR. SILVERMAN: If your Honor please, I believe that all of the causes of action are before you, and it was our contention in the context of this litigation, at the end of the plaintiffs' case, to make a motion to dismiss various aspects of the complaint, for whatever reasons then may exist, including lack of proof --

THE COURT: Is the third-party beneficiary claim before me?

MR. SILVERMAN: It is not part of the pretrial order.

THE COURT: Because I have not heard anybody urge that it was.

MR. ODELL: I certainly have not urged.

It was one of the complaints that were consolidated --

THE COURT: Can it be dismissed?

MR. SILVERMAN: I was going to dismiss, your Honor, just for the sake of good order and so that things

are really taken care of in totality, that at the end of Mr. Odell's case we would move to dismiss those counts on which no evidence had been offered.

THE COURT: All right. I'll await that event.

MR. SILVERMAN: Just so we can be sure we have it all out after I know what my friend is going to try for.

THE COURT: In any event, Mr. Odell, you do not propose to offer any proof on Count 3?

MR. ODELL: I do not, your Honor. Mr. Trynin, who is the author of that count in a separate lawsuit was here the opening day of trial and he hasn't been here since, and I don't want to speak for him because he is very sensitive about me dismissing something that he did.

THE COURT: Very good.

MR. ODELL: Your Honor, in your absence, may I read into the record some reference from Mr. Chernow's deposition which I am going to use so I can alert my owrthy opponents of additional portions of his deposition?

THE COURT: Why don't you just tell them?

MR. ODELL: Let me do it on the record, your Honor.

THE COURT: No, I think it more appropriate to tell them, because I should be here if the record is in

the course of being kept.

MR. ODELL: Let me do it when you get back.

(Recess)

(In open court)

Q Mr. Chernow, let me take you to the announcement of the sale of Buckingham by Schenley around November 1st of 1970.

Do you recall that the first announcement on the sale of Buckingham stated the closing would take place on December 31, 1970?

A I don't recall that specifically, no.

Q Well, do you recall that there were public announcements to the effect that the sale of Buckingham had been postponed from an earlier date to a later date in the period between November of 1970 and May of 1971?

A Yes.

Q And was there more than one of those postponements of a closing date?

A To my best recollection, there were.

Q And do you know what the reasons were for postponing those closings?

A It was my understanding that Northwest Industries, which was then in the process of trying to borrow funds from the financial community to pay the $120 million, was en-

countering difficulties in raising that sum of money.

Q Apart from the difficulties that you described with Northwest Industries raising the money, at the time of the announcement had Schenley received an indication from the Antitrust Division of the Department of Justice that it would consent to the sale of Buckingham to Northwest Industries?

A I have no specific recollection of that.

Q Well, do you recall that a time came when a ~~subsequent~~ consent decree was submitted to the Department of Justice for approval and signature regarding the sale of Buckingham, and can you tell me what day or date about that was?

A No, I have no direct knowledge of that.

Q Mr. Chernow, I have a copy of the minutes of Schenley as they were given to me by Haskins & Sells in the course of our review of their work papers --

THE COURT: If it's just a question of establishing the date, do you want to state what the date is? Is there any dispute about the date?

MR. ODELL: The minutes state that the antitrust decree was submitted to the Department of Justice on February 25, 1971, and its approval was expected within thirty days.

Q If the minutes say that, do you accept it?

A If the minutes say that, then I accept it.

Q One further question.

On the announcement is there any doubt in your mind as to when the sale of Buckingham was publicly announced?

I have a copy here which I will be glad to show you, that it appeared in the Wall Street Journal on November 2, 1970.

Would you accept that?

A Assuming there was no prior announcement, I have to accept it.

(Continued on next page)

Q No what?

A No prior announcement. I'd have to accept what you present to me.

Q Well, there was another announcement to the effect that Rapid-American was negotiating for the sale of Buckingham on October 26, 1970.

Will you accept that as a prior, what you call a prior announcement?

A If it appeared in the newspapers, I have nothing further to say.

Q My question to you is, in the month of November or in the month of October, did the market prices of Schenley common stock go up on the announcement of the sale of Buckingham for $120 million?

A I have no specific recollection of it but I would tend to doubt it.

Q Would you accept the statement of market prices as given to us by counsel for Schenley and Glen Alden that the market price range of the Schenley common stock in the month of October was a high of 28 and a low of 25, and in November it was a high of 26-1/8 and a low of 23-5/8? Will you accept those figures?

MR. SILVERMAN: Those are stipulated facts.

THE COURT: It is already in evidence, isn't it?

MR. ODELL: I don't think they are in this form, your Honor.

Q At the time the sale was announced and the making of a memorandum of an understanding that was introduced previously was accomplished, did the board of directors of Schenley, to your knowledge, have any discussions as to what was going to be done with the proceeds of the sale of Buckingham?

A Not to my recollection.

Q Do you personally, as the chief financial officer of Schenley, have any discussions with the president of Schenley or the chairman of the board of Schenley as to what disposition was to be made of the proceeds of the sale of Buckingham?

A I had no personal conversations with the president or the chairman of Schenley as to the disposition of the proceeds.

Q You recall the meeting of the board of directors on February 25th at which there was considered the proposal made by Glen Alden to merge with Schenley, is that correct?

A I didn't call it.

Q No, no, but you recall there was a meeting --

A Did I call --

Q Do you recall that there was a meeting of the

board of directors of Schenley on February 25, 1971?

A Yes, I do.

Q And that one of the subjects for discussion at that meeting was the proposal made by Glen Alden to merge Schenley with Glen Alden; do you recall that?

A Yes.

Q Now, my question is, before February 25, 1971, did you come to any judgments or conclusions as to whether, upon consummation of the sale of Buckingham, Schenley would have surplus cash, that is to say, surplus cash and marketable securities that were not needed for the day-to-day operations of the distilling business and the distribution of liquors?

A I don't recognize your term "surplus cash." In a business organization which is structured with short term debt, long term debt, accounts payable, the utilization of proceeds from whatever source have an approach in relationship to those indebtednesses which make your term superfluous.

I don't know what it means.

Q Well, assuming the cash on hand, the cash and marketable securities on hand was not necessary to meet any maturities of either long or short term debt, did Schenley have surplus cash on hand, assuming the sale was consummated

of Buckingham?

A Short term debt or our handling of short term debt is not based upon maturity dates. While we do make 90-day notes, they are reducible or prepayable without penalty and as cash proceeds come in, where appropriate, we reduce the amount of the short term debt.

Q Well, assuming the sale of Buckingham was consummated at the $120 million price, was it your plan as the chief financial officer and the planning financial officer to apply the proceeds from the sale of Buckingham to the reduction of short term debt?

A I had no specific plans for the projected proceeds from the sale of Buckingham.

Q To your knowledge, did any -- did Mr. Goldberg have any plans that he discussed with you?

A I am not familiar with --

Q Mr. Goldberg was then president of Schenley?

A Yes, he was.

Q Did Mr. Becker, who was chairman of the board of directors, discuss the question of the application of the proceeds of Schenley with you before the February 25th meeting?

A No.

Q Well, just let me carry this a little further

and I will go back to the meeting of February 25th.

Did there come a time when the Buckingham sale was closed and Schenley received the cash in Northwest notes in the amount of $120 million in payment for Buckingham?

A Yes, there came a time.

Q And that was about May 10, 1971?

A It was exactly May 10th.

Q At May 10, 1971, tell me what were your plans for the application of the moneys and marketable securities that came in from the sale of Buckingham?

A By May 10, 1971, the merger with Glen Alden's subsidiary had been announced and was in the process of being structured.

It was our plan to utilize some of those proceeds to purchase the debentures which would be issued to the Schenley shareholders.

Q At that point, how much in cash was to be used for that purpose, as of May 10th?

A We purchased -- in June we purchased --

Q I didn't ask you that. At May 10th, you said the deal was being structured.

How much in debentures at that time were you planning to buy?

When I say "you," I mean Schenley.

A At face value on the assumption that all of the outstanding stockholders would accept the cash and debentures, it would require the purchase of approximately 101 million face value debentures, or a cash payment to Glen Alden for those debentures of approximately $80 million.

Q Eighty?

A Eighty, yes.

Q We won't spend any time about a difference of a million or so more.

In addition to the purchase of the debentures, was Schenley to lay out some additional cash in connection with that merger?

A Schenley was to provide the outstanding Schenley's shareholders directly with the $5 in cash to the common shareholders and the $4.50 in cash to the preferred shareholders.

Q And assuming everybody accepted, as you said, that would total approximately $17 million, wouldn't it?

A Approximately.

Q So Schenley at May 10th or thereabouts was planning to pay out $98 million in connection with this merger, is that correct?

MR. SILVERMAN: If your Honor please, assuming that 100 percent of the shareholders took it.

MR. ODELL: Of course, assuming.

Q Is that right?

A That's correct.

Q Did the $98 million of cash as of May 10, 1971, assuming what Mr. Silverman said we should assume, did that amount of money represent surplus cash of Schenley?

A Again, I don't know what your term "surplus" means.

Q Was any part of that $98 million, according to your definition, going to be used to retire short term or long term debt?

A Not the $98 million.

Q And the $98 million was going to leave the treasury of the company, is that correct?

A Yes.

Q Did the discussion come up at all in which you were a party as to whether or not Schenley was in a position to pay out $98 million in cash without adversely affecting its business operations?

Did that question come up in any discussion in which you as chief financial officer was a participant?

A I don't know if it came up as a question. It was our feeling that Schenley could, by the continued prudent use of its assets, earn a fair return on the

invested capital.

Q As a matter of fact, if Schenley paid out that $98 million, it would reduce its invested capital by $98 million, so its return of capital would be higher to the extent you reduced capital by that payment, is that correct?

A Mathematically, yes.

Q Well, I mean just in a business sense, apart from mathematically, isn't that correct?

A If your earnings are up and your invested capital is down, yes.

Q Your ratio is better in terms.

Now, at May 10, 1971, was Schenley subject to any loan agreements with lending institutions which limited the amount of cash that could be paid out in connection with dividends or the acquisition of its capital stock?

A Yes.

Q And were those the loan agreements with the Prudential Insurance Company and a number of other companies who were participants in a loan of a total of $71,500,000 that was then outstanding?

A There was a larger amount outstanding but that particular segment of the long term debt, seventy-one million-five, was so restricted as to payment of dividends.

Q Yes, and there was another loan agreement, was

there not, that provided that if Schenley sold Buckingham and it had to pay off a loan which at that time was either 12-1/2 or $10 million?

A Correct.

Q So in addition to the $98 million that was going out in the merger, another ten or twelve million had to be used to pay off a loan whose terms required such a payment, is that correct?

A Yes. Two million of that were due that very same period and smaller sums were due within the next few years after that date.

Q But we are talking about $12-1/2 million, short and long term, that kind of loan?

A Part of that was due in 1971. Another part in 1972. To the extent of about $2 million in each of those years. I think, if my recollection serves me, the balance of two-million-five was due in 1975. That was by the action in connection with the Buckingham matter, we did pay off that particular segment of our long term debt.

Q I'm trying to determine from you -- and I'm sure this is due to some lack of communication on my part, not yours -- what the total amount of debt that was outstanding that had to be paid off on account of the sale of Buckingham.

Was it $12-1/2 million including long and short term debt?

A No more than that, yes.

Q Did any question come up whether Schenley could pay off that amount of the loan incident to the sale of Buckingham without adversely affecting its business operations?

A I think I have already addressed an answer to that question.

Q This is over and above the $98 we are talking about.

A Talking about the additional twelve?

Q The twelve that you had to pay out.

A I would have to say our discussions related to the totality of the disbursements.

Q So that would be 110 million?

A Right.

Q Now, in May of 1971, how much in 6 percent Glen Alden debentures did Schenley own?

A I would have to be refreshed on the exact amount.

Q Well, let's start with 1970, which shows in the annual report in the back of the proxy statement $13,784,126 at cost of Glen Alden 6 percent debentures.

Those debentures were purchased in 1969 and in

1970 by Schenley, is that correct?

A Subject to the amounts, those debentures were purchased either on the New York Stock Exchange or Over-The-Counter by Schenley.

Q So that -- I'll have the May 31st figure for you in just a second.

We were given a May 31st balance sheet which showed that as of May 31, 1971, and I will be glad to introduce it as Plaintiffs' Exhibit 17-B.

Do you see it there? It may be a little faint because --

A Yes, I see it.

Q It is a poor copy. It is $15,831,000 invested at cost in 6 percent Glen Alden debentures.

Now, was the almost $16 million that were so invested in 6 percent Glen Alden debentures cash that was needed or was not needed by Schenley for its business operations?

A It was an earning asset for Schenley.

Q I understand it produced interest income.

A Right.

Q But was that sum of money needed to be held as cash or marketable securities in the current asset side of Schenley's balance sheet as part of its working capital in

order to operate its business?

A I don't know what you mean by was it cash that was needed on its asset side.

Can you be more explicit in your question?

Q Could Schenley operate its distilling and other business operations in the liquor and spirits field without having this some $16 million in the form of cash or marketable securities that could be sold on short notice to meet the short term cash requirements of Schenley in the operation of its business?

A Yes.

Q Thank you.

THE COURT: Would you read that last question back, please.

(Question read.)

MR. ODELL: Your Honor, may I offer in evidence Exhibit 17-B?

MR. SILVERMAN: No objection.

THE COURT: Received.

xxx (Plaintiffs' Exhibit 17-B for identification received in evidence.)

Q Mr. Chernow, just so there is no difference between us as to semantics in my use of the words "surplus cash" -- can you hear me?

A Yes.

Q I defined what I thought was surplus cash with respect to this some $16 million of moneys invested in the 6 percent Glen Alden debentures.

Do you follow me?

A I hear you.

MR. SILVERMAN: I haven't followed that at all.

Q Did you follow me, Mr. Chernow? Then I will take care of Mr. Silverman later.

A I heard you. Are you redefining your use of the term "surplus"?

Q No, not at all.

THE COURT: He is giving you a definition and using that definition which you don't have to accept for more than the purposes of that very question.

You are not redefining that word for accounting purposes or for all time.

MR. ODELL: Are we waiting for an objection?

THE COURT: No.

Q What was the answer to the question?

A I don't know that there is a pending question.

THE COURT: Having established that as the definition for surplus --

Q Having established that as the definition of

surplus cash, is it fair to say at this point that at May 31, 1971, Schenley had the $98 million that was going out in the merger, the 12-1/2 that was going to be paid to the insurance companies and this 16 million, a total of $126 million in surplus cash on the defintion that I just gave you of surplus cash?

A I still don't like the use of the term "surplus." In the very narrow sense to which you applied it in the terms of the 16 million as a measure of alternate investment, I could find that acceptable. I am not sure that I understand the application here.

Q Well, do you have trouble with the application with respect to the 98 million that was going out?

A I have trouble with your use of the term "surplus."

Q Do you have a term that is used within the business circles of your company to define cash that is not needed, cash or marketable securities that is not needed for the purpose of meeting the current requirements of cash for the operation of Schenley's business?

A I know of no general, broad sweeping term that would apply.

Q I am not trying to argue with you. For want of a better word, isn't my definition of surplus cash a pretty good working definition?

MR. SILVERMAN: Objection.

A I will accept your word. I don't accept your complete definition, but if you will ask your question, I will be pleased to answer it.

Q If you accept my word, I have no questions more to ask on that question.

MR. LEVIN: I didn't know that the witness had accepted his word.

Q Okay. Now tell me what was the situation on May 30, 1971 --

THE COURT: Let me ask this. Is this still in the same area?

MR. ODELL: Yes, sir.

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THE COURT: Haven't we established all the facts with regard to the necessity for this money in the operation of the business that could be possibly established?

MR. ODELL: The necessity for this money by Schenley, your Honor?

THE COURT: Yes. Didn't Mr. Riklis go over this subject to some extent?

MR. ODELL: To some extent he did, your Honor. I think that this does, as far as I'm concerned, this pretty much wraps up for me the questions of surplus cash at this point.

THE COURT: If you have a couple of more questions and then we can go on forever to another subject, that would be great.

MR. ODELL: Yes, your Honor. I was starting to lead into a new area.

THE COURT: All right.

Q Did the loan agreements that Schenley had with the Prudential Insurance Company and other lenders that you described briefly before, did they limit the amount of cash that Schenley ~~had~~ could used for the purpose of acquiring its own capital stock?

A Yes.

Q At December 31, 1970, what was the limit on the

amount Schenley could use for capital acquisitions or payment of dividends?

A To my best recollection, the -- that sum of money in the restricted pool, as it was called, was approximately $80 million.

Q Had that amount grown by any substantial sum by May of 1971? Had the amount of $80 million, which you said was the limit on December 31st, grown to a larger amount by reason of the earnings and the sale of Buckingham in that five-month period beginning January 1st and ending May 31, '71, had it grown by any substantial amount?

A No.

Q In order to pay out this $98 million, was it necessary for Schenley to obtain the consent of its lenders, Prudential and others, to (a) consent to the proposed merger, and (b) consent to the payment of the $98 million that was proposed to be paid out by Schenley in the merger?

A To my best recollection, it was not necessary to obtain the consent to the merger because Schenley was the surviving corporation, but it was necessary to obtain their consent to make a distribution of $98 million which at June -- in June of 1971 would have exceeded the amount in the restricted pool.

Q What was done by you to obtain the consent to the payment of this $98 million by these lenders?

THE COURT: How does this bear on our disclosure issue?

MR. ODELL: Well, your Honor, I'm glad you asked that question because -- if you don't mind my saying so, I sort of feel like a suspect here trying to get away with a common law cause because I don't have a good non-disclosure case.

THE COURT: I'm just wondering why, on the disclosure issue, it was relevant to get proof the insurance companies had to consent to this. That's the only question.

MR. ODELL: The reason for it is, your Honor, that in the loan agreements or in the proxy statements they mention the fact that, subject to the applicable loan agreements Schenley will -- well, let me pick this phrase -- will transfer to Glen Alden substantial funds of Schenley, including a substantial part of the proceeds received by Schenley from the recent sale of its subsidiary, the Buckingham Corporation.

That's all they said subject to these loan agreements: "substantial sum of money," without saying how much. And I think I tried to explain in my opening statement that the question of surplus cash is not one that

the aferage investor can make a judgment about from reading a financial statement. That's an inside fact that bears on the value of a security --

THE COURT: No. I'm only talking about the question of the consent.

MR. ODELL: Let me go a little further, and you will see it.

What was the last question before the Court interrupted, please?

(Question read)

THE COURT: Answer.

A I must comment a bit on the phraseology of that question, with that last phrase, "by these lenders."

Q By the insurance companies who had lent -- who were the parties to the loan agreements with Schenley.

They were lenders, weren't they?

A Yes.

Q Okay.

A A member of our board of directors visited with the Prudential Life Insurance Company and described the program and, in the light of his historic relationship with the individuals at the life insurance company, because this director had been a commercial banker with a large New York bank, he visited with the Prudential in our behalf

and established the basis for the consent that we would obtain from them.

Q When did that take place, approximately?

A My best recollection would be that his first conversation with them took place sometime in early April of 1971; perhaps the end of March. I don't recall the exact date.

Q After that first conversation, did you play any part --

A Yes.

Q -- in dealing with the insurance company with respect to the consent and increasing the amount of money that would be permitted by the lenders to be used by Schenley for acquiring its capital stock?

A I'm not certain as to the timing, but I think in the original conversations there was a strict mathematical computation of outstanding shares times the needed dollars per share in establishing the initial consent from the insurance company. That was modified to provide for certain possible contingency, a cushion.

Whenever you negotiate --

THE COURT: Just a minute. We are getting awfully far afield unless there is some relevance in this to nondisclosure.

MR. ODELL: I am, your Honor.

Q Did --

THE COURT: Please. You said you were going to get to it in a question or two. You are now getting down to all sorts of -- little details of how the consent was obtained.

MR. ODELL: The proof will show -- it's all contained in letters -- that Schenley asked for and received the consent of these lenders to pay out for the acquisition of this minority position in the common stock -- in the stock of Schenley,the sum of $115 million, not $98 million.

THE COURT: All right. Then what?

MR. ODELL: Pardon me?

THE COURT: Then what?

MR. ODELL: Now, that fact was a consummated fact before this merger became effective. The application and the request for --

THE COURT: All that does is it gives them room to move up to that distance; right?

MR. ODELL: Yes, but, your Honor --

THE COURT: Then the question is whether or not the words "substantial sums" has some correlation within 80, 90, 100, 115; isn't that what we end up with?

MR.ODELL: The word "substantial" as used in the proxy statement could mean 20, 30 or 40 million. There is no definition of "substantial."

It was known --

THE COURT: You are eliciting these facts in order to argue that they knew ahead of time that they could draw up to 115?

MR. ODELL: And didn't tell the minority stockholders.

THE COURT: That it could be as much as 115?

MR. ODELL: $115 million.

THE COURT: Have we got that fact established now?

MR. ODELL: I would hope with the introduction of these letters and exhibits we will establish that fact, and I would say that we have at least accomplished something today, if we got that far.

THE COURT: Is there any question as to the authenticity of these letters?

MR. SILVERMAN: No objection as to authenticity. Which ones are you putting in?

MR. ODELL: I am introducing Exhibit 61, which is the original loan agreements plus the amendment dated June 17, 1971, which contained the consent of the lenders

to permit Schenley to pay as much as $115 million in connection with the acquisition of this minority position. I have a copy that's signed by --

THE COURT: Why don't you offer the letter?

MR. SILVERMAN: The date was when, June 17th?

MR. ODELL: June 7, 1971.

THE COURT: June 7th?

MR. ODELL: Yes.

THE COURT: The letter authorizing 115 was after the --

MR. SILVERMAN: After the date of the proxy.

THE COURT: So the 115 is established at a time after the word "substantial" has been used and, therefore, cannot have a bearing on -- they couldn't have put in 115 in place of "substantial" because they didn't have it at that point; is that correct?

MR. ODELL: Your Honor, they applied for it on April 21st.

THE COURT: But they didn't have it.

MR. ODEALL: I would like to say this, your Honor: If the disclosure of this information, if the event occurred --

THE COURT: Let's put the letter in. It's one letter. It's dated in June.

MR. ODELL: I offer in evidence Exhibit 61, which includes all the loan agreements, including one dated June 7, 1971.

MR. SILVERMAN: No objection.

THE COURT: Received.

xxx (Plaintiffs' Exhibit No. 61 was received in evidence.)

MR. ODELL: I offer in evidence a separate folder marked Exhibit 62 which is the correspondence between Schenley and mainly Mr. Chernow and the Prudential Insurance company and other lenders that begins on March 1, 1971, and goes through -- with respect to the loan and this other loan where they were going to pay off the 12 million 5, it goes through June 17, 1971.

THE COURT: All of those letters, do we need them all or do we just need that last one?

MR. ODELL: Your Honor, I think I'm going to need them all because if we get into any ruckus, one leads to the other.

THE COURT: Let's put in the one you count on. If there is a ruckus, you may want to offer another. As of this moment there is no ruckus.

MR. ODELL: I would like to put them all in. If I had a pick, I would offer -- I --

MR. SILVERMAN: It would be easier for you to consent to put them all in, rather than fighting about it.

MR. ODELL: Plaintiffs' Exhibit 62 offered in evidence.

xxx (Plaintiffs' Exhibit No. 62 was received in evidence.)

MR. SILVERMAN: Your Honor, that exhibit has been marked?

MR. ODELL: 62 and 63 has been marked.

MR. SILVERMAN: Your Honor, I think it would be proper at the time the exhibit is marked and is in evidence to call your Honor's attention to the fact that on June 16th one of the institutions consented, so that I just merely want to establish that there was a document that indicates that consent was not there at the time of the proxy statement.

MR. ODELL: May I finish my offer, your Honor, and then I can answer Mr. Silverman.

Exhibit 63 are these original loan agreements before they were amended in the respects that are shown in Exhibit 61, and I offer them in evidence. These are the agreements between Schenley and the Prudential and the various other lenders on this long-term loan.

MR. SILVERMAN: No objection.

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xxx (Plaintiffs' Exhibit No. 63 was received in evidence.)

MR. ODELL: Your Honor, may I say that the June 16th letter to which Mr. Silverman refers is found in 62, Exhibit 62, and is a letter to one of the lenders that had $7 million of this entire loan, and I believe -- well, I won't go into that because I would just be -- all right.

Your Honor, I would like to say that the law is quite clear, and there are some very recent decisions, including the Court of Appeals in this circuit that says that if any substantial change in information comes to the knowledge of the issuer of a proxy statement before the merger, that information has to be disclosed and, if necessary, in an amendemtn to the proxy statement.

THE COURT: I am going to recess for the evening and we will resume at 10:30.

MR. ODELL: Your Honor, I'm going to need Mr. Chernow some more. I am sort of left hanging with some other witnesses at this moment, and I may want to interrupt his testimony if it's with his permission only to put some of these witnesses on for a very short time tomorrow.

MR. SILVERMAN: Which witness?

MR. ODELL: You will see what witnesses they are. They are not defendants. You will learn tomorrow.

MR. SILVERMAN: I will respond at the time.

THE WITNESS: Well, is my time that free?

THE COURT: Off the record.

(Discussion off the record)

(Adjournment taken to October 16, 1975 at 10:30 a.m.)

Exhibit 2 is the proxy statement of the merger between Schenley and Buckingham to which there is no objection at all. It's been marked as 2 for identification. I offer it in evidence.

THE COURT: It will be received.

xxx (Plaintiffs' Exhibit No. 2 was received in evidence.)

MR. ODELL: There is also a group of exhibits which break down a good many of the details of the annual reports which were admitted in evidence yesterday for each of those periods --

THE COURT: Do we need to discuss these at this point?

MR. ODELL: Well, if there is going to be any objection -- the only objection I know of is relevancy.

THE COURT: Why don't we go ahead with the witness, unless you need one of these exhibits as you go along, at which point you can put it in with the flow of the proof.

MR. ODELL: You prefer I keep moving. Very good.

DIRECT EXAMINATION CONTINUED

BY MR. ODELL:

Q We closed yesterday after we had introduced a letter agreement of June 7, 1971 between Schenley and Prudential concerning the amendment of the loan agreement,

and one of the provisions incorporated in that amendment was increasing the amount available for purchase of the acquisition of the shares of Schenley from -- to $115 million; do you recall that?

A Yes.

Q And I would like to sk you, who was it that suggested the $115 million figure in the request for that amendment in that amount?

A I don't recall who suggested the $115 million. It was a natural number in looking at the total package.

Q It was done at the instance of Schenley, wasn't it, one of its officers or directors?

A I would say so.

Q Can you tell me what the basis was for arriving at that particular figure?

A I think I indicated yesterday that if you took an exact calculation of the outstanding shares and multiplied that by the proposed price for each of those shares, you would come to a very specific, exact amount.

Now, when you deal with an insurance company or any financial institution, you always allow room for variances that may take place, either for a cushion above the exact amount or to allow for certain other possible contingencies.

Q What were the other contingencies that were considered in connection with raising the amount from $98 million, which was the merger figure -- merger price figure at the time, to $115 million?

A I'm sure there were a number of items, but included certainly would have been the fact that an interest rate does not remain locked in permanently, and part of the cushion which we had to address ourselves to was the possibility that interest rates would vary, or might vary.

In that event, certain variations from the original exact amount would have to be encountered in calculating the total withdrawal from the restricted pool under the Prudential agreements.

THE COURT: Interest rates on what?

THE WITNESS: If you are offering a debenture with a certain value, that value is related to the then interest rate.

If, for example, that bond or debenture is faced with a rapidly rising market in terms of interest rates, a higher interest rate is applied, or would have to be applied, in calculating the value of that bond.

Since you would have to apply a higher interest rate, and this is a discount bond, you would, in effect, be reducing the value of that discount bond by virtue of

the fact that the interest rates have gone up.

Therefore, to be prepared for that possible contingency, and certainly nobody can anticipate what the interest rates in the market place, and that's the total market place, will be, we made provision for that possibility.

Q Roughly speaking, you were there trying to make provision for a possible increase in interest rate between what dates in 1971?

MR. SILVERMAN: Your Honor, I must rise to object. I thought that your Honor had ruled yesterday that the disclosure aspects of all of this were in a sense comprehended by the dates, and that the proxy statement had gone out admittedly before these negotiations, that this restructuring or revision in the agreements had taken place long after the proxy statement had gone out.

And I thought that your Honor indicated that further evidence on this subject, in this vein, is not probative of any issue in this case.

THE COURT: What say you to that?

MR. ODELL: Your Honor, I remember that question being raised and I pointed out to your Honor that any change in conditions prior to the actual date of the merger, under the decided cases in this circuit, would require an

amendment of a proxy statement, if those changes materially changed the kind of disclosure that would be required.

As I recall, your Honor nodded your head, at least, with knowledge of those cases that permitted that.

THE COURT: Even assuming that, this is not a change. This is a question of how a figure got arrived at and it has already been established in the record that that figure got arrived at and when it got arrived at, so we are not talking about a change. We are only talking about the factors that went into that, and you have established for your record that there was a figure sought for clearance from the banks and sought on a particular day.

It turns out that that happens to be after the date of the statement.

MR. ODELL: The request was made much before the statement.

THE COURT: I know, but they hadn't gotten it. At best, it is arguable that from your point of view they should have amended and said, "We had asked for $115 million."

MR. ODELL: That's right.

THE COURT: Mr. Silverman is saying what difference does it make, what relevancy does it have to non-disclosure what the factors were, what the contingencies were

that went into the 115, because those do not involve a change. They involve events after the proxy and, in effect, he says it's irrelevant.

I am trying to see where it becomes irrelevant. It is not a change,obviously. At most it's a factor in something that's happened and you have established that fact in this record already.

MR. ODELL: Do you want me to address myself to relevancy?

THE COURT: Yes, I do. The earlier one, I don't see that that answers it.

MR. ODELL: Your Honor, one of my principal faults that I have to pick with this proxy statement is that it gave no indication whatsoever in the body of the proxy statement as to how much surplus cash Schenley had, and the fact that the existence and the amount of the surplus cash that's been the subject of the testimony here is the kind of fact that insiders would know about and outside stockholders would know nothing about it. They would not be in a position to form a judgment.

THE COURT: That has nothing to do with the last question that was asked.

MR. ODELL: Had this proxy statement disclosed the fact that this company was negotiating or was planning

or had requested an increase from the $79 million or $80 million that the loan agreements permitted at the end of 1970 to $115 million, that would have, in itself, been a disclosure to the public of the amount of surplus cash there was in this company.

Mr. Chernow testified that the $98 million that was going out, which was not disclosed in the --

THE COURT: It still has nothing to do with the contingency that is a merest detail of this whole picture.

MR. ODELL: Your Honor, there are any number of prospectuses and proxy statements where a company is required to state what its intentions are with respect to material facts. Now, if you are going to talk in proxy statement on the first page with respect to subject to applicable loan agreements, and those very loan agreements have a limitation at the time, and those loan agreements are the subject of an intention by the management of the company to increase the amount substantially from the $79 or $80 million to $115 million, I say that's a material fact that should have been disclosed in this proxy statement.

THE COURT: We have that in the record already. We have that in the record.

MR. ODELL: Yes.

THE COURT: Why do we need this detail? How does this detail advance your cause at all?

MR. ODELL: Well, I'm trying -- there are several reasons. I am trying to get from this witness the fact that the increase to $115 million that was sought was, in itself, an expression of the amount of cash this company could pay out, subject to the contingencies that he is talking about, or any other contingencies he may bring out.

THE COURT: That's something else, and you didn't ask that. I am addressing myself to this specific objection.

Mr. Odell; I'm going to sustain that objection. If you want to go on to the question you last put, do. I am going to sustain that objection.

Q Besides the interest rate reason for asking for this increase to $115 million, were there any others?

MR. SILVERMAN: Objection.

THE COURT: Yes. Sustained. In the same area.

Mr. Chernow, was the asking for $115 million a statement of opinion on your part, as you now sit here, that you had $115 million that you could utterly just dispense with?

THE WITNESS: We could not utterly dispense with

$115 million.

MR. ODELL: May I continue in the vein of the question you just asked, your Honor?

THE COURT: The one that I just asked?

MR. ODELL: Yes.

THE COURT: You may.

Q Mr. Chernow, was the $115 million an amount that Schenley was prepared to pay out in cash in consummation of this merger?

MR. SILVERMAN: Would you have the question reread, sir?

THE COURT: Yes.

(Question read)

A It was an outside number that we requested from the Prudential Insurance Company. Whether or not the contingencies of the market place, had it caused the amount to reach the $115 million, I really cannot tell you, sitting here now, whether we were or were not or would or would not have at that time paid that sum of money.

Q I have one more question to ask you about. Under this agreement of June 7, 1971, the amount of cash under the language of the June 7, 1971 letter was the fair market value of such debentures at the time of acquisition?

MR. SILVERMAN: Would you show the witness the

document?

MR. ODELL: Sure.

Q Do you see that?

A Yes.

Q With the further proviso that the aggregate amount of all such cash and cost to the company of such debentures shall be deemed to be restricted payments and the phrase that does not follow -- I'm sorry -- you have seen the sentence that reads, "For cash not exceeding the fair market value of such debentures at the time of acquisition, provided the aggregate of the amount of such cash and cash cost to the company of such debentures shall not exceed $115 million."

Do you see that?

A I see it.

Q If the interest rates had gone up, would that increase the amount of cash Schenley would have to pay out? If the interest rates had gone up and Schenley were to buy these debentures at fair market value, if interest rates had gone up, would Schenley have to pay more money for these debentures?

A That's implicit, in fact, explicit in the description I gave you before.

(Continued on next page)

Q But if interest rates had gone up and the face amount of the debentures had been reduced or a higher interest rate was provided, I'm assuming that the situation was instead of a 7-1/2 percent rate on these debentures that you bought at a fair market value of 80 percent of their principal amount, if that interest rate was increased to 9 percent and interest rates had not increased in the market generally, would not the fair market value of the debenture have been increased? Wouldn't the discount have been reduced?

A First of all, I think you are intertwining a number of unrelated issues as they address themselves to the description of bond discount.

The question of interest rates going up does not necessarily change the coupon rate of the bond.

What does happen is that the discounted current value of that bond goes either up or down. Now, if the interest rates go up, a 7-1/2 percent bond in comparison with the rest of the marketplace would, therefore, have a fair value of less than it would have had at the prior level of general interest rates.

Q If the interest rates had gone up and the interest rate on the bond was increased --

A That is a lot of if's.

Q -- wouldn't you have the same fair market value?

MR. SILVERMAN: If your Honor please, this is argumentative questioning.

MR. ODELL: Your Honor, I am trying to explain the functions of the money markets on the cost to Schenley of buying these debentures and I think maybe I am elaborating the obvious here, but fair market value is a function of interest rate and principal amounts and that is all I'm trying to get this witness to say.

MR. SILVERMAN: I thought we were talking about the contingencies that they were providing against.

THE COURT: I thought that also.

Q Had the management of Schenley made any decision in the event interest rates had gone up to increase the face amount of these debentures?

A To increase the face amount of these debentures?

Q Yes. If the interest rates had gone up.

A No.

Q Well, let me go on to the next portion of this letter amendment which permits -- the second amendment is paragraph 3-A of this June 7, 1971 agreement -- which permits the excess of Schenley's consolidated current assets over the sum of its consolidated current liabilities and consolidated long term debt to be less than $170 million.

Would you read that, please.

A Yes.

Q As I understand that paragraph and the portion from which paragraph 6 of the original agreement says, Schenley shall not do certain things, and one of the things they can't do by this amendment is permit an excess of its current consolidated -- of its consolidated current assets to exceed by more than $170 million its current -- it is the other way around, I'm sorry -- that its current assets must exceed its current liabilities and long term debt by at least $170 million.

Is that a fair reading of it?

A That is what it says.

Q It doesn't quite say that here but by reference to the earlier agreement, it would do so.

Would you tell us how the figure of $170 million was arrived at?

MR. SILVERMAN: Objection, your Honor.

THE COURT: How is this relevant?

MR. ODELL: Your Honor, it is my position that this figure of $170 million, that is to say, that this company has to have a working capital of $170 million between its current assets and its current liabilities plus its long term debt, and that that is a judgment by the insurance

company as to what is the permissible minimum from the standpoint of the security of its loan of current assets that must be maintained by this company in the form of working capital.

THE COURT: Assuming you are right, how does the insurance company's opinion of what it wants the company to have as working capital, how does that affect the disclosure in this proxy statement?

MR. ODELL: Your Honor, it does not but it bears on the question of surplus cash and the determination of the amount of surplus cash.

THE COURT: I sustain the objection. I don't see that. The insurance company's opinion as to what they want as protection for their loan -- that is what it amounts to, isn't it?

THE WITNESS: Yes, sir.

MR. ODELL: It is also the insurance company's opinion of what is adequate working capital --

THE COURT: Maybe it is but I will not treat that as having a bearing on the issues before me.

I will sustain the objection.

Q Mr. Chernow, when for the first time were you told about the Glen Alden offer to merge with Schenley in 1971?

A At a board meeting of Schenley Industries on February 25, 1971.

Q And who informed you that that matter was to be taken up at that board meeting?

A Mr. --

MR. SILVERMAN: I'm sorry. I will object to the question --

THE COURT: You first learned at the board meeting?

THE WITNESS: Yes.

THE COURT: So you went to the board meeting not knowing?

THE WITNESS: Correct.

THE COURT: All right. Sustained.

Q I am looking at the minutes of that board meeting, a part of Exhibit 64 for identification.

I ask you first, who introduced the proposal of Glen Alden to merge with Schenley at that board meeting?

A Mr. Becker, chairman of the board of Schenley Industries.

Q I will ask you to have these minutes before you. I have a copy at my desk and we can go on from there.

I will ask you to look at the third paragraph on the second page of those minutes which commences with the

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MR. ODELL: I'm sure it is not your voice. It is my hearing.

THE COURT: I'm sure it is.

Q Did Mr. Becker in the course of his presentation advise the board the basis upon which the terms of this merger as outlined by him in these minutes were arrived at by Glen Alden?

A The basis of the terms --

Q Just so there is no mystery about that, the paragraph we passed talked about each share of Schenley common stock would be converted into a $30 principal amount of a new 7-1/2 percent debenture and $5 in cash.

Did Mr. Becker advise the board on what basis that amount, the conversion price, was arrived at?

A Conversion price?

Q Yes. That is to say, the $5 and the $30 principal amount of debenture per share of common stock.

A I don't recall a specific detail as to how the individual components of the package were structured, but in --

Q You don't recall his telling the board that, is that right?

A I don't recall his describing in detail the individual components of the package to be offered for the

outstanding shareholders.

Q Did he describe it generally, in something less than detail?

A Yes.

Q What did he say?

A He talked of providing the outstanding Schenley common shareholders with a package whose value would be approximately 29, and that the one for 1.40 preferred shareholders would get 9/10 of that package given to the common shareholders.

Q Did he tell the board by what criteria or standards or means that he arrived at that $29 package for the common?

A I do recall that he did comment and there was discussion that 29 was a reasonable and fair price in the light of the history of the outstanding securities over the recent period of years.

Q I don't quite understand your allusion to the history --

THE COURT: No, just a minute. He is testifying as to what somebody told him. It is not his allusion.

MR. ODELL: I was trying to move along a little faster. Sorry.

THE COURT: All right.

MR. ODELL: Would you read the witness' reply, please, Mr. Court Reporter.

(Answer read.)

Q Did he make any mention as to how many years of history he was referring to?

A I don't recall a specific enumeration of number of months or years, but it was --

Q Did he describe or refer to the history of the earnings of Schenley? Is that the history he described as being the one you referred to?

A No. I referred to the value placed on the shares of the stock in the public marketplace.

Q And you understood him to be then referring to the market prices as quoted on the New York Stock Exchange for the common stock, is that correct?

A Valuation in terms of market price for the securities.

Q Did he talk or mention valuation in terms of any factors other than market price?

A I don't recall a specific mention of other factors.

Q Were there any other factors, considerations that he referred to or mentioned that Glen Alden had used in arriving at this $29 package for the common stock?

MR. SILVERMAN: Objection, your Honor.

THE COURT: Yes; no foundation?

MR. SILVERMAN: No foundation and I thought that the prior testimony was to this effect:

He said, what were the factors that he mentioned that went into the setting of the terms, and the terms were -- by Mr. Becker and it was a Glen Alden proposal to Schenley, as you will see in the minutes, so I think this is completely repetitious.

THE COURT: Let me hear the question back.

(Question read.)

THE COURT: Any other factors other than those you testified to already?

THE WITNESS: None.

THE COURT: No other factors.

Q There were no other factors mentioned by Mr. Becker besides --

A Not to my best recollection.

Q After Mr. Becker outlined this proposal, did a discussion take place between the directors and Mr. --

A Yes, it did.

Q Can you tell me what questions, if any, you asked of Mr. Becker with respect to the value of this Glen Alden package?

MR. SILVERMAN: Does this go to the question of disclosure, your Honor?

THE COURT: I don't see how this is relevant. Perhaps there is some relevance that escapes me or that you plan to show, but I don't see why what questions he asked has any relevance to the issues in this litigation.

MR. ODELL: As to disclosure, there are several, your Honor.

I believe if there were no other factors considered by this board of directors or by Glen Alden in fixing the terms of this merger that were brought to the attention of the board of directors of Schenley, who had the veto power over this merger, that the proxy statement should have said that the value of this package was determined by market price and nothing else.

I think stockholders are entitled to know what their directors used or what considerations they took into account in arriving at the value of this package that is being offered in this proxy statement, whatever they are, and if market value was the only one, I contend that should have been in the prospectus, in the proxy statement.

MR. SILVERMAN: He has that in the record if that is his contention.

THE COURT: The question you asked does not go

to that.

MR. ODELL: I'm trying to bring out what was discussed by the other directors after Mr. -- what questions were asked by the other directors after the proposal, the outline of this proposal had been made by Mr. Becker. Maybe that is a roundabout way of getting into that question.

There are a number of questions that follow from that one. That is not the only one I have in mind.

I think I am entitled to know a number of other things about what was discussed by the directors of Schenley, what was raised by the directors of Schenley in arriving at their approval as it was given in this meeting of the board of directors.

THE COURT: What is your recollection of the discussion, Mr. Chernow, by the directors?

THE WITNESS: At this moment in time, it is hard to relate who said what, but the general tenor was a review of the reasonableness and fairness of the price.

Don't forget that all of us had lived with that security for -- or many of us on the board had lived with that security for many years. We felt an intimacy in terms of our own appraisal of what the reasonableness was of its value.

We took the position, though, that we were not

only going to count on our own feelings, attitudes and opinions, that we were going to seek the advice and counsel of investment advisors to review and affirm, if that were the case, as to the reasonableness and the fairness of the offer.

We also reviewed in discussion the mechanics of -- or attempted to understand the mechanics of a merger because -- and counsel did at that time indicate to us that we, Schenley, would be the surviver of a merger with a wholly owned subsidiary of Glen Alden, as a result of which we became a wholly owned subsidiary of Glen Alden.

That was especially important to me in the light of our financial agreements that mergers were okay, so to speak, without prior approval to the extent that Schenley was the surviving corporation, and there were many comments along the way about, one, the issue of value as we just described it, and the mechanics of the merger and comparably related factors.

THE COURT: Go ahead.

MR. ODELL: I didn't hear the last sentence.

THE COURT: Comparably related factors, comparably related factors.

Q Let's start with the last one first.

What were the comparably related factors that

were discussed?

MR. SILVERMAN: Objection, your Honor.

THE COURT: Do you have those in mind?

THE WITNESS: No, sir. If I had them, I would have been more explicit.

MR. ODELL: Have you ruled, your Honor?

THE COURT: He answered. He said he didn't recall specifically what they were.

2 Q Did any director present ask whether the amount
3 of Schenley's cash and marketable securities at that time
4 were taken into consideration in fixing this value?
5 MR. SILVERMAN: Taken into consideration by whom,
6 by Glen Alden?
7 MR. ODELL: By Glen Alden.
8 A Not to my recollection.
9 Q Did any director raise the same question with
10 respect to the existence and amount of Schenley's surplus
11 cash with respect to the value of these shares for merger
12 purposes?
13 A I don't get your question.
14 THE COURT: Would you read it again.
15 (Question read.)
16 A Not to my recollection.
17 Q Did any director of Schenley present at that
18 meeting express any objection to the proposed price for this
19 package?
20 A No. In light of the fact that the propriety of
21 the price was going to be reviewed and counseled by
22 investment advisors, it was not a final determination at
23 that moment in time. It was something that the directors
24 could review and regard again upon receipt of the investment
25 advisors' comments.

2 Q Did any discussion take place at that meeting as
3 to who would be the investment advisor?
4 A I don't recall the mention of a specific name.
5 Q Were there any names mentioned?
6 A I don't recall the mention of any names.
7 Q Did the board discuss at all the manner in which
8 the investment advisor would be selected?
9 A I don't recall a determination by the board at
10 that time of the manner in which an investment advisor would
11 be selected.
12 Q Was someone authorized --
13 A Yes, the chairman of the board, to my best
14 recollection --
15 Q The chairman of the board was what?
16 A Pardon me?
17 Q I asked, was someone authorized to --
18 A To my best recollection, the chairman of the
19 board would attempt to engage investment counsel to so
20 advise the board.
21 Q Was the chairman so authorized at that meeting to
22 do so?
23 A I have to make the presumption that he was. I
24 don't recall specifically a motion but I'm sure that would
25 have been a logical authorization.

Q Did the name of Allen & Company come up at all at that meeting?

A I think I just indicated that no names of any investment counsel were discussed, to my recollection.

Q Mr. Chernow, do you recall that at that very same meeting, the financial statements of Schenley were reviewed by the board of directors?

A Yes; I do have that recollection, yes.

Q The minutes that were given to me by Schenley those that you have before you -- and they make no reference to the discussions of the financial statements of the company at that meeting -- all that is attached to the minutes of that meeting, that I was given, at least, is an authorization to announce the earnings of Schenley for the year ended 1970, is that correct?

A I have not reviewed this line-by-line --

Q Would you please? I am showing you what was given me.

A If that is what was given u, that is all I can address myself to.

Q Attached to the minutes of that meeting --

MR. SILVERMAN: Mr. Odell, I'm sorry, may I look at what it is that you have in your hand?

MR. ODELL: What I have in my hand is a copy

attached to those minutes, I believe, of an announcement of the 1970 earnings of Schenley.

MR. SILVERMAN: Your Honor, as I understand it, Mr. Odell made a request of us to supply him with those portions of the minutes that dealt with the merger. Those he got. We did not furnish him with a full set of the minutes, but I believe that he has a full set of the minutes and the full set of the minutes does reflect the fact that Mr. Chernow distributed the financial reports at that meeting.

MR. ODELL: I'm not quarreling with that, your Honor. I'm merely trying to say, for the purpose of the witness -- I'm trying to get the witness to tell me about what discussions took place with respect to the financial statements of Schenley, and I was going to show him the minutes that were given to us by Haskins & Sells as part of the work papers that our accountants examined in this case and included a full set of those minutes.

If I may, with Mr. Chernow's counsel's permission, I would like to stand here with a single copy of these minutes and ask the questions.

Q At the tail end of the minutes of this meeting that I have before you, there is a heading here called Financial Report, and a reference to Mr. Chernow

2 distributing financial statements of this corporation
3 and consolidated subsidiaries for the year ended
4 December 31, 1970, and the minutes goes on to refer to
5 a general discussion in which all directors present
6 participated, took place, general discussion, that is,
7 with respect to that financial statement.
8 The financial statement that you presented to
9 the board of directors, was that the financial statement
10 that's found in the annual report that was given to the
11 stockholders of Schenley, which we previously identified
12 here as Exhibit 9? And I will show you 9 if you will just
13 give me a second.
14 A It was not this specific item as marked as an
15 exhibit. It was the internally-processed report which
16 I distributed since this is printed after the auditors
17 have, so to speak, signed off, so that it was not this
18 particular document which you identified as one exhibit
19 or another.
20 The basic numbers as indicated here of the net
21 income of $27,183,000 and sales of six six nine are as
22 printed ultimately in this report.
23 Q But you had before you an internally-prepared
24 report, and I ask you whether Plaintiffs' Exhibit 15 for
25 identification is that report that you had before you.

A Essentially it appears to be.

MR. ODELL: I offer that report in evidence as Plaintiffs' Exhibit 15.

MR. SILVERMAN: No objection.

THE COURT: There being no objection, it will be received.

xxx (Plaintiffs' Exhibit No. 15 was received in evidence.)

Q Mr. Chernow, was there also -- was there a summary analysis of operations for the year ended 19- -- December 31, 1970 submitted to the board at the same time?

A I don't know what you are referring to.

Q Mr. Chernow, I was not given --

MR. SILVERMAN: Objection, your Honor.

Q I will show you Plaintiffs' Exhibit 20 for identification which is a report entitled Summary Analysis of Operations for the Year 1971, and is a comparison with that of 1970.

My question is: Looking at Plaintiffs' Exhibit 20, which refers to the year 1971, was there a similar report given to the board of directors for the year 1970?

MR. SILVERMAN: Your Honor, does that question imply that that was given to the board in '71?

MR. ODELL: Not at all. I asked -- it doesn't,

2 to answer your question.

3 A I have no recollection that this detail sheet

4 which you identify as Summary Analysis of Operations was

5 given to the board in either -- in connection with either

6 the operations of 1970 or 1971.

7 Q But, Mr. Chernow, you are familiar with a report

8 that was prepared under your supervision that bears --

9 A That's a different question.

10 Q I am not quarreling with you.

11 A Oh.

12 Q -- that bears the title Summary Analysis of

13 Operations?

14 A Yes, I am familiar with it.

15 Q Was such a report prepared for the year 1970?

16 A I have to presume it was.

17 Q May I ask you another question with respect to

18 the report for 1970?

19 A Certainly.

20 Q I'm going to show you and ask you one question

21 with respect to Plaintiffs' Exhibit 19 for identification,

22 which is headed Schenley Industries Consolidated Profit

23 and Loss by Operation, and it shows 1970 actual.

24 I'll ask you to look at that report and tell

25 me whether the figures that appear in each of those columns

under those column headings for the year 1970 is the summary of operations report for Schenley for the year 1970?

A The column identified as 1970 actual in a budget plan prepared sometime during 1971 as it relates to the following year, 1972, which is the content of this paper, appears to be the actual as reported for 1970.

Certainly, looking at the bottom line, I am not in a position to compare individual numbers along the way.

Q And one more question with respect to the report we identified as Plaintiffs' 20 for identification entitled Summary Analysis of Operations for 1971, which compares the results of that year with the preceding year, would you say the figures shown in 20 for identification relating to the calendar year 1970, as compared there to 1971 figures, is an accurate statement of what that report for the year 1970 shows?

MR. SILVERMAN: If your Honor please, I am confused. I thought I heard the witness identify that as a budget plan in which one column represented actual figures.

THE COURT: That's the earlier exhibit.

MR. SILVERMAN: Is this a different exhibit?

MR. ODELL: This is going back to the '71 exhibit

2 that compares -- sorry, I will speak louder.

3 MR. SILVERMAN: No, no, I misunderstood you.

4 I heard you.

5 A This is a report comparing 1971, the year

6 ending December 31st, with the year ending December 31,

7 1970, on an actual basis.

8 MR. ODELL: Your Honor, I offer Plaintiffs'

9 Exhibit 19 for identification as well as 20 for

10 identification in evidence.

11 MR. SILVERMAN: I don't understand the purpose

12 of the offer, your Honor.

13 THE COURT: Do you offer more than the column that

14 you had the witness refer to?

15 MR. ODELL: No, sir.

16 THE COURT: The purpose of the offer is what?

17 MR. ODELL: The purpose of this offer is to

18 discuss with this witness, first, the increase in the

19 earnings of Schenley for the year 1970, and what particular

20 departments and operations of Schenley contributed to those

21 earnings in 1970.

22 I will also use it when I get to a discussion

23 with this witness of the same questions as they relate to

24 the year ended December 31, '71.

25 THE COURT: I will permit those columns in

evidence. To the extent the witness has identified those exhibits, they are in. The balance is excluded.

xxx (Plaintiffs' Exhibits Nos. 19 and 20 were received in evidence.)

THE COURT: Is this a good time for our mid-morning recess?

MR. ODELL: Yes.

(Recess)

(Continued on next page)

2 Q Mr. Chernow, would you look at Plaintiffs' 20
3 which shows the Schenley earnings for 1970, excluding
4 Buckingham, and the comparison of those same earnings with
5 the year December 31, 1969, and you will notice that the
6 1970 earnings were $18,311,000 as compared to $15,028,000
7 in the preceding year.
8 MR. SILVERMAN: What exhibit are we talking about?
9 MR. ODELL: Exhibit 20 -- I'm sorry, 15 for
10 identification.
11 A That is what it seems to be here, 15.
12 MR. ODELL: It's been received in evidence.
13 Q Do you see those figures?
14 A I see those figures.
15 Q Now, this report, you said, was discussed with
16 the directors at that February 25th meeting.
17 Did any discussion take place with regard to the
18 improvement that took place between the 1969 and 1970
19 earnings of Schenley alone?
20 A I can't recall specifically but it is a normal
21 practice -- it is my normal practice quarterly and annually
22 when these reports are prepared for the board of directors
23 to review performance as to sales, expenses, bottom-line
24 figures, and I would have to be quite sure that I did go
25 through that normal process of reviewing the operations at

2 that point in time.

3 Q The minutes showed that the board of directors

4 at that one meeting authorized, one, the release of

5 Schenley's 1970 earnings; second, the announcement that it

6 had approved, in principle, at least, this merger with

7 Glen Alden, proposed merger with Glen Alden, subject to the

8 opinion of an investment banker.

9 The third thing that happened in that minute was

10 that the New York Stock Exchange was advised of these

11 announcements that would be forthcoming and trading was

12 stopped in the stock.

13 Are you familiar --

14 A I am not familiar with it in the context in which

15 you presented it.

16 Q Put it in the context in which you understood it.

17 A At the beginning of the board meeting, Mr. Becker

18 indicated to us that just prior to the board meeting, he had

19 called the appropriate listing officer of the New York Stock

20 Exchange to hold trading in these shares pending completion

21 of our board of directors meeting.

22 Q Did any of the directors present object to Mr.

23 Becker's action in so advising the New York Stock Exchange?

24 A I'm quite certain no one did. There would have

25 been no basis for anybody to make such an objection.

2 Q After the discussion of the merger and the
3 reference to the advice given to the New York Stock
4 Exchange, now that we got these earnings, did any
5 discussion take place with respect to the earnings of
6 Schenley at that point in the meeting as to whether the
7 announcement of the merger, the stopping of trading and the
8 announcement of Schenley's earnings all take place in --
9 practically on the same day? Did any discussion take place
10 as to the propriety of that action?
11 A I can't recall any such discussion. I don't see
12 there is a sequitur in which you say.
13 Q More specifically, the 1970 earnings of Schenley,
14 excluding Buckingham, were some 20 percent higher than they
15 were for the year ended 1969, is that correct?
16 A I did not calculate the percentage. For
17 Schenley?
18 Q Excluding Buckingham.
19 A They were eighteen million three-eleven. And
20 for the prior year they were fifteen zero-two-eight.
21 Q So, roughly about nineteen and twenty percent?
22 A That is your calculation.
23 Q My question is, in view of the fact that the
24 board had earlier been told that the terms of the merger
25 were fixed by market prices, did any director raise any

2 question about announcing the terms of this merger at the
3 same time that these increased earnings would be announced?
4 MR. LEVIN: I object, if your Honor please. I
5 believe this is argumentative.
6 THE COURT: He is asking what was said about it.
7 MR. LEVIN: There is a preface to his question.
8 MR. SILVERMAN: He said, in view of the fact that
9 the merger terms were set exclusively by --
10 MR. ODELL: I will revise the question, your
11 Honor.
12 Q Mr. Chernow, in your experience --
13 THE COURT: No, please. Let's stay with this
14 time. Anything said on this subject by any director, we
15 are stopping tradding, we are announcing the merger and
16 giving out the new figures all at the same time and these
17 new figures are higher?
18 THE WITNESS: I recall no such comment.
19 Q No such discussion.
20 THE COURT: Was trading resumed? When was it
21 resumed?
22 THE WITNESS: It would have been resumed upon the
23 release of the announcement of the merger and the call to
24 the -- which would have been made directly by telephone call
25 to the listing officer and simultaneously be placed on the

2 Dow Jones tape. So that would have been immediately after
3 the board meeting.
4 THE COURT: Trading was halted for what, two or
5 three hours?
6 THE WITNESS: I would guess so, yes, sir.
7 THE COURT: All right.
8 BY MR. ODELL:
9 Q According to the May 21, 1971 proxy statement of
10 Schenley, there is a statement that the closing price on the
11 New York Stock Exchange on February 25, 1971 was $27-1/2 per
12 share for the Schenley common and $25 for the preferred and
13 the day before, the closing prices were $29 and $26-7/8.
14 Do you know what facts, if any, were responsible
15 for the drop in price on the close of trading on February
16 25th of the Schenley common shares?
17 MR. SILVERMAN: Objection.
18 MR. LEVIN: Objection.
19 THE COURT: How is that relevant, even assuming
20 he is in a position to know? Is this a market assessment?
21 MR. ODELL: Your Honor, I think the main
22 relevance of this is the announcement of this merger with
23 the merger terms fixed a ceiling on the price of Schenley
24 stock thereafter.
25 It is our contention that if the improvement of

2 earnings had been announced before the merger was announced,
3 the market price would have reflected an increase in price
4 based on an 18 percent increase in earnings.
5 MR. LEVIN: If your Honor please, this is a
6 disclosure --
7 MR. SILVERMAN: The prices are disclosed in the
8 proxy --
9 THE COURT: I sustain the objection.
10 Q Mr. Chernow, let's go now to the March 25th
11 meeting of the board of directors.
12 I show you the minutes of the meeting of March
13 25, 1971 of the board of directors of Schenley as they were
14 given to me.
15 You have the second page of those minutes before
16 you where the reference is made to the selection of an
17 investment advisor?
18 A Yes.
19 Q And there is a reference to the number of
20 discussions concerning the selection of an investment
21 advisor in the second line under the heading there of,
22 "Retention of Investment Advisor." It refers there to
23 discussions concerning the selection of an investment
24 advisor to this corporation.
25 Discussions between whom are referred to in that

reference?

A I really couldn't say.

Q Between the February 25th meeting and the March 25, 1971 meeting, were you consulted by Mr. Becker as to the selection of an investment advisor for Schenley?

A Between those dates?

Q Yes.

A I did have a conversation with Mr. Becker between those dates wherein he indicated that he thought that Allen & Company might be engaged as investment advisor.

Q When was that meeting?

A Somewhere between February 25th and March 25th.

Q And somewhere between those two dates, had you had any conversations with any representatives of Allen & Company with respect to their engagement as an investment advisor to the company?

A Somewhere in the early part of March -- that is approximately the best I could place it at this point -- in a discussion with Mr. Becker, I was requested to cooperate with Allen & Company in providing them with our historic financials and to be as cooperative with them in providing them with whatever information they might require so that they could approach a thorough presentation to the board.

Q Can you be more precise in fixing the date on

which this conversation took place with Mr. Becker?

A I would have to say it was probably within the first two weeks of March, possibly. I really cannot recall the exact calendar at that point in time, but that would be my best recollection.

Q Shortly after that meeting, were you telephoned or in touch with Allen & Company about carrying out Mr. Becker's request that you --

A I was.

Q And approximately how long after your conversation with Mr. Becker did that conversation take place?

A Possibly the same day, possibly the next day, depending upon whether the appropriate indivdual was there when -- whether he was there when I called or whether I was there when he called. I really can't define the specifics of the communication.

Q In that first meeting, with whom was that telephone conversation?

A It was a telephone conversation with Mr. Stan Shuman of Allen & Company.

Q How soon after that telephone conversation did you begin to give him information as requested by Mr. Becker?

A Probably as soon as the information was available. Presumably in the nature of annual reports, it was immediately available from our file and I could have them delivered to him immediately.

Q Was there any information besides annual reports that Mr. Shuman requested that you give him?

A He did inquire as to any information we might provide regarding the performance of our brands, regarding anything that I might have in my file by way of newspaper clippings about the company, magazine articles. He indicated he wanted to get a feeling for what makes the company tick.

Q Did he ask you for any information concerning the inventories of Schenley?

A I recall that he probably did, yes.

Q Tell us the kind of information he requested.

A To my best recollection, it was a schedule of -- a breakdown of the components of both our bulk inventory in the United States, in Scotland, in Canada, our case goods inventory, an indication of our material in process which we developed internally for basically management purposes.

Q Was this conversation about inventory at the same time that Mr. Shuman made his initial requests of you for annual reports, and so on?

A I had a number of telephone calls with Mr. Shuman and to my best recollection, although I can't place that exactly in point of time, I did see Mr. Shuman from time to time, either in his office or in mine.

Q These meetings in person with Mr. Shuman at either his office or yours, did they all take place between that date sometime in March that you referred to and the meeting of the board of directors on March 25, 1971?

A I had a number of meetings but if you are asking me did I cease seeing or talking to Mr. Shuman at March 25th, my answer is no.

Q I'm sorry, maybe my question might have not been too clear.

My question was, did the meetings that took place between you and Mr. Shuman in fulfillment of the instruction of Mr. Becker to give him any information he wanted, did all of those meetings take place prior to March 25, 1971?

A I have to presume that those meetings pertinent to his report on the 25th would have taken place prior to March 25th.

Q You also testified with respect to documentary information concerning Schenley that you gave Mr. Shuman, and my question is, by March 25, 1971, had you given him all

the documentary information he requested concerning Schenley?

A To my best knowledge and recollection, I gave him whatever information he requested.

Q By March 25th?

A By March 25th.

Q What was your understanding of what Allen & Company's function, as personified by Mr. Shuman, what was the function to be performed by Allen & Company -- and I will put it to you in this way:

Were they engaged for the purpose of advising the board of directors of Schenley what was the fair value of the Schenley common shares and $1.40 preferred shares for the purpose of this proposed merger?

A To my best recollection, they were engaged to review whether our offer was fair and reasonable and whether or not they had any modifications to the proposed offer that they might recommend to the board.

Q When you say "our offer," you are referring to Glen Alden's offer, aren't you?

A No.

Q Who initially made the offer to merge, Schenley?

A Schenley did not make the offer to merge. We talked of -- when I said "our offer," we had already indicated at the board meeting of February 25th that there

would be an offer to the outstanding Schenley stockholders, our stockholders, of a particular package.

We indicated, too, that we, the board of directors, agreed to it in principle subject to a review by investment counsel as to fairness and reasonableness.

I don't know that it was not, therefore, our offer.

THE COURT: Mr. Chernow, if I can go back to something:

When during the course of the year of 1970, you released quarterly figures, unaudited figures, that was your practice?

THE WITNESS: That was our normal practice.

THE COURT: You released nine-month figures, I'm sure.

THE WITNESS: Yes.

THE COURT: Would the investor or would the market be able to glean from the nine-month figures the rough area that the year would end up at?

THE WITNESS: That might be difficult, sir, in this sense:

Ours is not a calendar or fiscal year of equivalent months. We do have a seasonality in our business and it becomes an unknown until the gift-giving and the

Christmas buying have their particular impact on our sales.

THE COURT: Go ahead.

MR. ODELL: Your Honor, the financial statements we introduced show quarterly earnings --

THE COURT: I appreciate that. I got an answer to the question I asked.

BY MR. ODELL:

Q Was the fee to be paid Allen & Company discussed at the March 25, 1971 meeting?

A I don't recall.

Q Well, were you told prior to March 25, 1971, what the Allen & Company fee was going to be?

A Prior to March --

Q Prior to the meeting.

A I don't recall the point in time that I knew of the size of their fee.

Q Is it fair to say that at the time of the board meeting on March 25, 1971, you did not know what the size of their fee was to be for the advice they had given?

A I say I can't recall whether I did or not.

Q Was there any discussion at this meeting regarding any indemnity that would be given by Schenley to Allen & Company in connection with any opinion that it might give pursuant to the request that was going to be made of

them?

A I'm not aware of any such discussion.

Q As long as I am on the subject of fee, did there come a time when you learned what that fee was going to be?

A Yes.

Q When was that?

A I indicated previously I don't recall the point in time.

Q Mr. Chernow, did you receive printer's proofs of the proxy statements relating to this merger?

THE COURT: Mr. Odell, are we going to litigate the size of the fee as having some bearing on the consideration for an allegedly improperly favorable report, because, otherwise, what difference does it make?

MR. SILVERMAN: The fee was disclosed, your Honor, in the proxy statement.

THE COURT: I'm curious as to why we are getting into this at all.

MR. ODELL: I'm going to drop that subject because my case doesn't depend on any of those innuendoes.

Q Let's get to the meeting of March 25, 1971, the minutes of which are before you, at which Allen & Company represented by Mr. Shuman was present at the meeting, is that correct?

A Yes.

Q And he was introduced at that meeting as being the investment advisor and after the board ratified his selection and retention as the investment advisor for Schenley, as shown in those minutes, the meeting proceeded to a discussion with Mr. Stanley Shuman of Allen & Company and that is summarized, at least in the first paragraph of the minutes as you have them before you under the heading, "Suggestions of Allen & Company, Incorporated," is that correct?

A Yes.

Q Now, you see the last sentence of that particular paragraph reads as follows:

"Attached hereto is a statement furnished by Mr. Shuman to the secretary subsequent to the meeting summarizing his remarks."

Would you look at those minutes and tell me whether you have such a statement furnished by Mr. Shuman attached to the minutes?

A Yes, I do.

Q What is the date of that statement?

A June 3, 1971.

Q Let's go on with the suggestions that are described in the portion of the minutes that immediately

follows that reference to the statement. You see there -- your Honor, to spare you the job of looking at this, I would like to summarize this quickly to keep you current with what we are talking about.

First, Mr. Shuman suggested that the debentures mature which fourteen rather than fifteen years.

Second, that the sinking fund requirements be 3-1/2 percent a year for the first five years and then 5-1/2 percent for the second five years, and so on.

At the February 25th meeting, was any reference or any discussions --

MR. SILVERMAN: Do you want to go through the balance of --

MR. ODELL: I will but I would like to take these one-by-one in reference to what was discussed at the meeting at which the merger was approved in principle.

Q At the February 25th meeting, was there any discussion with respect to what the sinking fund would be on these debentures, 7-1/2 percent debentures?

A I have no specific recollection of whether the details of the sinking fund were discussed.

Q Did you know at the time you voted to approve in principle the terms of this merger at the February 25th meeting that the debentures would have a sinking fund of

any kind?

A To my recollection, yes. There was to be a sinking fund. It was to be a 7-1/2 percent coupon. It was to be 15 years.

However, beyond that, I don't recall the specific minutia of an indenture or proposed indenture.

(Continued on next page.)

Q You also knew, as the February 25th minutes mention, that the debentures were to be senior to the 6 percent debentures of Glen Alden that were outstanding; is that correct?

Item 3 of Mr. Shuman's suggestion was that the new debentures be pari passu as to subordination with the existing Glen Alden 6 percent debentures in 1988.

My first question is, did any discussion take place with respect to Mr. Shuman's suggestion that these 7-1/2 percent debentures be made pari passu rather than senior to the 6 percent Glen Alden debentures?

A I don't recall a specific discussion, but I do recall a general concept that they couldn't be made anything more than pari passu with these 6's of '88.

Q Was any reason given for that? Why they couldn't be --

A To my knowledge, it must have been in the indenture of the 6's of '88.

Q Now, let's read on with these minutes.

These are the four points, the fourth point being that the holders of the debentures be permitted to apply the debentures in part in payment of the exercise price of the public traded -- publicly traded warrants issued in the future to purchase capital stock of Glen Alden.

Now, after those changes were suggested, the minutes state there was a general discussion of Mr. Shuman's report by all the directors present.

Would you tell me whether Mr. Shuman, after outlining his suggestions, gave the board at that time the basis for his opinion that the terms with these suggested changes would be fair and equitable to Schenley?

A I can only recall the overall concept and reaction that the terms were fair and reasonable, and that the changes that he recommended would tend to strengthen the attractiveness of the debenture to be issued.

Q Did Mr. Shuman mention at all what were the considerations upon which he based the opinion as to fairness? Did he give any -- that's the question.

A I am sure he gave a general review. I don't recall specifics or that he detailed his thought process.

Q Did he tell the board of directors, for example, that the reason why he tought the terms of the merger with these suggested changes were fair and equitable was because they were -- they reflected the current market prices of the Schenley stock?

A I am sure he must have made some mention of current market prices, but I don't recall his specific tie-in as you describe it.

Q Well, do you recall that he gave any explanation, even though you can't recall the details of what he gave or any description of the reasons for his having approved, believing this merger to be fair and equitable?

A I am sure that there was some presentation as to the composition of his thoughts of fairness and reasonableness, but I cannot recall details.

Q Would you look at that June 3, 1971 letter, which is appended to the minutes, first for the purpose of refreshing your recollection as to any of the details given by Mr. Shuman at the March 25th meeting for his -- to support his opinion that the terms of the merger were fair and equitable?

A Is there a question pending?

Q I asked you to read that June 3rd letter, which is a four-page letter, to refresh your recollection as to those things -- as to those considerations that were mentioned by Mr. Shuman at the meeting of March 25th to support his opinion that the terms of the merger were fair.

THE COURT: Does the letter contain such a statement? Is there any dispute about it?

MR. SILVERMAN. The document speaks for itself.

THE COURT: Do we need to ask this witness what his recollection of the meeting is if the letter contains a

statement of what it is? Unless you dispute it.

MR. ODELL: I might very well dispute it, your Honor.

MR. SILVERMAN: "Might very well" is not enough.

THE COURT: I don't see any point in having the witness read a four-page letter on speculation of that kind.

MR. ODELL: I would have no way of knowing what Mr. Shuman told this board of directors orally on the basis of which they approved this merger, and so I must rely on Mr. Chernow's recollection to the extent he has it, as to what were the bases for his decision. I wish it were otherwise, and I wish I could say that this letter said it all. I can't say it.

THE COURT: All right.

Mr. Chernow has read the letter.

What is your recollection as refreshed, if it has been from that letter, as to what was told to you?

THE WITNESS: I think what I indicated before about his general discussion of fairness and market price and -- is only confirmed by what I have read. I think it spells out what I attempted to convey in my response to an earlier question.

MR. ODELL: Your Honor, may I offer in evidence

the minutes of February 25, '71 and the minutes of March 25, 1971 of the board of directors?

MR. LEVIN: What numbers are those?

MR. ODELL: That's Exhibit 64, which contains a number of other minutes, including these minutes.

MR. SILVERMAN: What are you offering to put into evidence?

THE COURT: The entire minutes of the two meetings that have been the subject of discussion.

MR. SILVERMAN: Just those two meetings?

THE COURT: Yes.

MR. SILVERMAN: The document, I think, may contain other minutes, and I take it you are not offering those.

MR. ODELL: Mr. Silverman, to answer your question, the document 64 does refer to additional minutes. At this point I am offering only, and we had better mark this 64-A, being the minutes of those two meetings as they were given to me, and then what I would like to introduce as 64-B are the minutes of Schenley for the year 1971 in their entirety, as they were given to me by Haskins & Sells.

MR. SILVERMAN: For the year 1971?

MR. ODELL: Yes.

MR. SILVERMAN: I will object. There are two minutes or two board meetings that have been the subject of

this dicussion. I have no objection to the minutes of those board meetings being introduced, including, as I take it, an appendix to one, which is the June 3rd letter.

THE COURT: That will be received.

What about the meetings for the entire year '70?

MR. ODELL: '71, sir.

THE COURT: '71?

MR. SILVERMAN: After the merger?

MR. ODELL: Your Honor, let me --

THE COURT: That has nothing to do with this witness at this point, does it?

MR. ODELL: The only thing that has to do with the witness at this point in this batch of minutes given to me by Haskins & Sells is that it also contains the meeting of the stockholders of Schenley at the June 17, 1971 meeting of stockholders that passed on this merger.

MR. SILVERMAN: We stipulated that the merger became effective immediately after the meeting of the stockholders. This is a disclosure case.

THE COURT: At this point I think this offer is out of time in any event, and I am going to sustain it at this point.

MR. ODELL: I won't press it.

MR. LEVEIN: If your Honor please, this entire

line was permitted upon Mr. Odell's representation to your Honor yesterday that he was going to establish some sort of a conspiracy involving the management of Schenley and/or Glen Alden and Mr. Shuman, and I should like to ask Mr. Odell through your Honor whether, on the basis of the testimony that has thus far been elicited from this witness, he persists in that representation.

THE COURT: I don't think I will put that question to him at this point, but I will sustain the objection to the minutes for the entire year as without foundation as of this point, and untimely on this witness.

Let's keep going with this.

MR. ZULACK: May we mark the minutes for the two meetings?

THE COURT: They are in evidence.

xxx (Plaintiffs' Exhibit No. 64-A was received in evidence.)

MR. ZULACK: You have no dispute about the Haskins & Sells longer minutes?

MR. SILVERMAN: The short version or the long version, if they have the minutes of the two meetings we talked about, I have no objection.

THE COURT: Very well.

Q Did there come a time when you saw an affidavit

of Mr. Shuman sworn to on June 7, 1971 -- I believe was the date -- in the proceedings entitled David J. Green & Company, plaintiffs, v. Schenley Industries, Inc., and I show you that affidavit.

THE COURT: In the interests of saving time, what do you have in mind to do with this affidavit?

MR. ODELL: Your Honor, I'd like to answer that question but I'd prefer not to answer it in the presence of the witness.

THE COURT: All right, sir, would you go through the back door, please?

MR. ODELL: I seldom have had to do this, but this is getting to the point that Mr. --

THE COURT: All right.

(Witness temporarily excused)

MR. ODELL: This affidavit which the witness --

MR. SILVERMAN: Could we hear you, too?

MR. ODELL: This affidavit of June 7th provides the detailed reasons given by Mr. Shuman for determining that this merger was fair and equitable and it will detail a number of grounds for his opinion to that effect, most of which are to diminish the value of Schenley on a number of grounds, rather than to point to those actual facts which I will bring out in the course of this testimony,

I hope, and from additional witnesses.

THE COURT: How do you propose to use this exhibit in connection with this witness? That's my question.

MR. ODELL: I intend to ask this witness some questions as to whether or not some of these grounds given by Mr. Shuman for arriving at his conclusion were in fact true.

THE COURT: There is no reason why you can't do that as a factual -- as a matter of factual determination. You can ask him whether a certain facts was so, to his knowledge, or whether another fact was so.

MR. ODELL: I can do that, your Honor, but the other thing I wanted to do with these minutes, once I had --

THE COURT: In this affidavit.

MR. ODELL: In this affidavit.

-- is to ask him whether Mr. Shuman raised any of these matters --

THE COURT: You may ask him that, too.

MR. ODELL: You asked me what use I intended to make. That's two of the important uses I intend to make of this affidavit. It's the only thing extant I know of that tells us --

THE COURT: You want to ask him what his knowledge is about certain underlying facts that Mr. Shuman has relied

on and you want to ask him whether certain things Mr. Shuman said he relied on were brought up at the March meeting. Very good.

Bring the witness back.

MR. SILVERMAN: Your Honor, before we call the witness back, Mr. Shuman's affidavit was put in in a litigation in Delaware responsive to allegations by another expert. Not everything in that affidavit is the substance -- necessarily the substance of his opinion. In other words, this was a battle between experts on the issue of fairness and the factual materials that are involved, I respectfully submit, go to the issue of fairness. I still do not understand the disclosure aspects of this.

If there are disclosure aspects, if the thrust of this is that Mr. Shuman was a consummate liar, and we knew it, or that Mr. Shuman's statements were false or wrong and we knew it, and if it is further shown that the specific falsity was the predicate for the opinion given to the board, not a contest between experts in a Delaware lawsuit -- do you see how remote this is getting from the issue?

THE COURT: I see.

Mr. Silverman raises a good point here. What do

you say to that?

MR. ODELL: Your Honor, I don't know whether you saw the June 3rd letter of Mr. Shuman to the board of directors.

THE COURT: I did not.

MR. ODELL: If you would look at it first -- I say this preliminarily on the basis of a further remark I want to make. If you look at that ~~affidavit~~ letter, you will find it speaks in the most general terms of a whole variety of matters that he says he considered, without telling you anything about the weight he gave them, what the facts were relating to those criteria of value that he talked about. There is no detail there that a board of directors as knowledgeable as this one is, as Mr. Chernow testified -- there is no detail in that letter from which a knowledgeable board, acting in good faith and not on the orders of the controlling stockholder here, would have raised a number of questions with Mr. Shuman at that meeting, had he outlined the basic facts and considerations upon which --

THE COURT: Let me go to the tip of the iceberg here.

MR. ODELL: I am getting ready for that. I am not here, your Honor, to make a liar out of Mr. Shuman or anybody else. I'm here complaining about a proxy statement

that contains this language:

"The investment banking firm of Allan & Company, Incorporated, has acted as advisor to the board of directors of Schenley in connection with the proposed reorganization and has advised the board that, in their opinion, the terms of the proposed reorganization are fair and equitable."

I say that that language, to the average public investor, means that an investment banking firm has been engaged to advise this board of directors that the terms of this merger are fair and equitable, and my further position is that --

THE COURT: Then what?

MR. SILVERMAN: And they so advised them.

THE COURT: The fact is they did advise them.

MR. ODELL: Yes, and the fact is that he advised them on the basis of facts and other information concerning the business, and the affairs and earnings of Schenley, its inventories and so on. They advised them -- he based his opinion on facts that were incorrect, that were not true, and had the board of directors of this company acted as they were requi4ed to act, as normal, honest board of directors, they could not possibly have accepted this opinion by Mr. Shuman, and would not have put this statement in the proxy --

THE COURT: I will certainly permit you to inquire as to the facts in the Shuman affidavit of June as to whether or not they are as the witness understands them to be, assuming that he is in a position to answer that as to figures that are now four, five years old. That would seem to be clearly appropriate to inquire on, but as to getting into all of these details --

MR. SILVERMAN: Your Honor, I don't quarrel with that. That is, if the facts are in error, that he may establish. What that has to do, if they were honestly in error, assuming they are, and I don't believe they are in error, I don't understand where it takes him if they are in error, absent somebody having misled him, somebody having conspired with him.

THE COURT: This is a part of the proof. Maybe the rest of the proof will fail, and maybe the error will be de minimis.

MR. SILVERMAN: My friend said he is not challenging Mr. Shuman's honesty.

MR. ODELL: I said --

THE COURT: The second rubric of questions had to do with what he had told the board --

MR. ODELL: At the March 25th meeting.

THE COURT: I don't see -- unless this further refreshes the witness' recollection -- that that's an appropriate use of this affidavit with this witness.

So we are going to recess until ten after 2:00.

Bring Mr. Chernow back.

At ten after 2:00 you may inquire into the underlying facts by saying, "Isn't this a fact?" "What do you know about this fact?" "What do you know about that fact?" "What do you know about the other fact?"

We will go from there.

(Luncheon recess)

*****

2 lzmch Chernow-direct

Q Mr. Chernow, under the new management of Schenley, did you consider the record of the earnings growth of Schenley, of that new management, as compared to that the of the industry generally, was distinctly unimpressive?

MR. SILVERMAN: I object to the question.

THE COURT: I am going to sustain it as to form unless there is some foundation for the use of that form.

MR. ODELL: Your Honor, I will withdraw the question.

Q Mr. Chernow, was the growth rate of Schenley's earnings under its new management better than it was under the last five years of its old management?

MR. SILVERMAN: Objection, your Honor.

If he would like the growth rate, let's get the figures.

THE COURT: Don't we have the figures?

MR. ODELL: We have the figures that go back to about 1964, as far as I recall, plus some that I believe are -- I really haven't examined them, going back further.

THE COURT: Isn't that better evidence than this witness' tsetimony on that subject?

MR. ODELL: Let's see if I can get to the point of my question a little differently.

Q Prior to March 25, 1971, did you and Mr. Shuman discuss the growth rate of Schenley's earnings under its new management?

A I may have discussed with Mr. Shuman what the earnings actually were in prior periods.

Q At the March 25th meeting of the board of directors of Schenley, did Mr. Shuman tell the board of directors of Schenley that, in his opinion, the growth rate of Schenley was unimpressive?

The question is, did he say that to the board of directors?

THE COURT: Did he say that?

A I don't recall that statement by Mr. Shuman at the board of directors meeting.

Q Do you recall that the growth rate of Schenley's earnings were discussed at all by Mr. Shuman with the board of directors in that March 25th meeting?

A I think there may have been a discussion of -- or a comment by Mr. Shuman in talking about the price level of Schenley during the period long past to date, some discussion of price-earnings multiples, but I don't really recall a specific comment by Mr. Shuman that I can reconvey to you at this point.

Q Well, one more question on that subject of earnings

growth rate.

Did Mr. Shuman tell the board that, in his opinion, those earnings -- Schenley had a poor earnings growth rate?

A I don't recall such a statement by Mr. Shuman.

Q One more question.

Did Mr. Shuman tell the board of directors at that meeting on March 25th that, in his opinion, the record of Schenley's earnings in the five years preceding the end of 1970 was a poor record of growth?

MR. SILVERMAN: Objection, your Honor. I thought we were here to establish facts with respect to the materials in the document that my friend wants to talk about.

I consider this line not responsive to your Honor's direction.

MR. ODELL: Your Honor, apparently my understanding was that (a) I would go into facts, but I would also go into what was discussed and what was said by Mr. Shuman to the board of directors at the March 25th meeting of the kind that should have alerted the board of directors to the improper basis for his opinion as to the value of Schenley.

MR. LEVIN: Then I will object, your Honor. That is not at issue.

THE COURT: I thought we had determined that that

latter area was not in issue.

I am not quite clear. I think the ground has a little bit shifted from before lunch, and that -- because I remember ruling out one area of inquiry, and I'm not quite sure it's the same area any more.

MR. ODELL: Maybe the reporter can straighten us out on that point.

THE COURT: Why do you contend it is relevant, what he said?

MR. ODELL: It seems to me Mr. Shuman is now talking to a knowledgeable board and he doesn't have to quote chapter and verse in terms of fact as to his opinion.

THE COURT: And then what?

MR. ODELL: Well, if in fact he said to the board that his opinion was that the record of its earnings of Schenley in the last five years was a poor record, it seems to me -- and that that was one of the bases for his opinion that those terms of the merger were fair and equitable, it would seem to me that the board of directors would have to dispute that, and there would have to be some kind of disclosure made in this proxy statement that Mr. Shuman's opinion that the terms of this merger were fair and equitable were based on erroneous facts or -- there would have to be some disclosure that would qualify

Mr. Shuman's opinion and the reliability -- and the reliance that could be placed on it by any stockholder.

THE COURT: Let me see this affidavit.

And your question, in substance was whether or not he used the words "poor growth record"?

MR. ODELL: Right. Well, that was -- yes, that was the last question.

THE COURT: To the board in March of 1971, whether he used that language.

MR. ODELL: That's right.

THE COURT: It seems to me, taking an overall view of what he is really saying, as you read the balance of his affidavit, he points out in certain areas the market share dropped and in another area the increase in case sales was a disappointing increase, and then he specifically points out that most of the increase occurred under new management, so it doesn' seem to me that, even if you got that characterization, you really had anything.

I'll permit you to ask the question.

Was that said at the board meeting of March 25th -- March whatever, 1971, in substance, that Schenley had a poor growth record in recent years?

THE WITNESS: I don't recall that statement, sir.

MR. SILVERMAN: Your Honor, I merely suggest that

this affidavit, which was prepared in June in a litigation is what my friend is using to -- for the basis -- as the basis for his questions with respect to a communication to the board in March of '71.

THE COURT: Well, as I see what Mr. Odell is driving at here, he is saying that Mr. Shuman arrived at his determination that this was an appropriate price by saying Schenley was in awful shape. Schenley, according to his understanding of where it was going, was in fairly rosy shape, and, therefore, from that he wants me to draw the conclusion that the Schenley board permitted this opinion to issue based upon a gloomy prediction, when they knew the prediction was in fact partially rosy.

Am I summing it up correctly?

MR. ODELL: Your Honor, you said it better than I said it so far.

THE COURT: That's what he is getting at.

MR. SILVERMAN: I do understand that. I would merely observe --

THE COURT: Therefore, in effect, it was a quasi fraudulent opinion letter.

MR. SILVERMAN: My friend can argue from the facts what he will argue, but the word "poor earnings record" is a conclusion. The facts from which one can derive or

not derive that conclusion is what were the earnings.

THE COURT: I thought I made that clear about three minutes ago in terms of --

MR. SILVERMAN: Now my friend is examining into Mr. Shuman's conclusion rather than the existence of the underlying facts.

THE COURT: Mr. Silverman, I just asked him -- I just permitted him through me to put the question to the witness whether that conclusory language was used at the board meeting. The answer was "no." And I think I expressed an observation that I wasn't quite clear that it was even appropriate to ask the question because the rest of the paragraph explained what was meant by that language in hard facts.

Q Under the new management of Schenley, Mr. Chernow, did the number -- did the volume of case sales of Schenley increase between 1967 and 1970?

MR. SILVERMAN: Your Honor, there was no new management of Schenley in 1967.

MR. ODELL: I am comparing it against the old management.

THE COURT: Under the new management did the total case volume increase?

THE WITNESS: To use your term, "new management" --

MR. ODELL: Excuse me, your Honor, I think I can rephrase that question.

THE COURT: This is after Mr. Becker came in as chairman of the board, was there an increase in the total volume of cases sold?

THE WITNESS: Yes.

THE COURT: Mr. Odell, may I ask what it is you are looking for?

MR. ODELL: I am waiting for an exhibit.

THE COURT: What are you looking for?

MR. ODELL: I am looking for financial statements --

THE COURT: If it's a question of what the increase was, don't the --

MR. ODELL: The amount of the increase.

THE COURT: Won't those exhibits speak for themselves?

MR. ODELL: They would.

THE COURT: Do you need this gentleman to confirm that's what the exhibits say?

MR. ODELL: I guess not, your Honor. I think perhaps I was trying to summarize for you what the actual figures would show.

THE COURT: I noted a figure in the affidavit that you handed me.

MR. ODELL: Okay, I'm sorry.

Q Mr. Chernow, in August of 1968, were Schenley's inventories of whiskeys and productive capacity greater in relation to sales than then was the case in the industry in general?

A It was my opinion at that time that that was the case.

Q Was that the case in 1970, at the end of 1970?

A It was still my opinion in 1970 that that was the case.

(Continued on next page.)

THE COURT: Given what you were selling, you had more inventory on hand and more productive capacity than you needed, is that what you are saying?

THE WITNESS: As compared to my impression of what the others had.

Q When did you make that determination as to the condition of its inventory in relation to sales with respect to the year 1970?

MR. SILVERMAN: If your Honor please, he said it was his opinion, not a determination.

I would ask my friend to rephrase his question if he can.

Q When did you come to that opinion?

A Having lived in this industry for quite a number of years, you accumulate feelings, impressions, knowledge, data, all of which you use at some point in time to come to a more concrete impression or feeling.

There was no single moment in time when the light shown and I realized that that was a state of fact. It was an accumulation of background and data which I was in possession of.

THE COURT: Do I understand that the problem you have grappling with this situation is that you are distilling now for several years ahead?

THE WITNESS: Yes, sir.

THE COURT: And therefore, even if you were to change your view about what inventory should be carried, you may not effect an enormous change in that relationship for several years?

THE WITNESS: That's correct.

THE COURT: I understand, all right.

Q My question was directed to what the inventory situation was in the industry in general.

Did you understand that in the two questions I asked?

A That was not my impression of the thrust of the question.

Q Let me put the question again because I thought the question did refer to the industry in general.

In 1970, at the end of 1970, did you believe that the inventories of whiskey and the productive capacity of Schenley was greater in relation to its total sales than was the case in the industry in general?

A Generally during 1970, yes.

Q And did you have that same opinion with respect to the period of -- 1968 and the last four or five months of 1968?

A So far as 1968 was concerned, the impression was

greater than it was in 1969, which, in turn, was greater than it was in 1970. Or to say it another way, I felt decreasingly so as the years went by from 1968 to 1969 to 1970.

Q What was your belief on that same question at the end of 1971?

MR. SILVERMAN: Objection, your Honor. We are talking about a March 23,1970 meeting.

MR. ODELL: I'm not talking about a March 1971 meeting at all. I'm talking about facts.

THE COURT: This affidavit whose underlying facts you are plumbing, it speaks as of July of 1971. I would think that --

MR. ODELL: June.

THE COURT: June would be a cut-off time for any question in that area.

Q Well, what was your opinion on that question at the end of May of 1971?

A By 1971, it was my feeling that we were not noticeably or significantly different in relation to the needs for our sales than the rest of the industry in terms of inventories or plant capacities.

Q In mid-1968, did you have an opinion as to the distortions as to quantity or age of Schenley's inventory of

bulk bourbons?

MR. LEVIN: I object to the word "distortions," your Honor. I don't know what it means.

THE COURT: Yes, objection sustained.

Q Is the word "distortions" as used in the liquor industry with respect to quantities of inventory and age of inventory, a word of common usage in describing excesses in terms of age or quantity?

A To my knowledge, the word "distortion" is a singularly applied term. It has no universal application in the liquor industry as against any other industry.

Q Well, is it a term that you have used in --

A Yes, I have.

Q And in what sense do you use the term "distortion" in referring to the age or volume of Schenley's bourbon inventory?

A Out of balance with the most desirable standard.

Q The most desirable standard being what?

A Being the situation where you have -- you have been that prescient that you are in a posture where you have exactly the number of gallons you need maturing at exactly the day when you can bottle it in the exact proportions related to the individual brands to which they are applied so that there is an exact quantity of bulk whiskey bottle

ripe at a day when you can bottle it and sell it. That is the ideal.

Q Well, based on that ideal state that you have described, did Schenley have distortions in its bulk inventories in mid-1968 or in August 31, 1968?

A That was my feeling.

Q By the end of 1969, had those distortions as to age and quantity been reduced?

A They had been reduced somewhat, yes.

Q By the end of 1970, had they been further reduced?

A They had been further reduced.

Q And by May of 1971, were there steps being taken to continue the reduction or elimination of these distortions?

A There are constant steps daily to so manicure that inventory that you can adapt it to a bottle-ripe posture.

Whether it means reduction or whether it means planning a different category of whiskey, that is an on-going thing and we do it constantly.

Q Well, now, in relation to the industry in January, would you say -- first, what information did you have with respect to the existence or non-existence of these distortions in inventory with respect to other companies in

the distilling industry, at the end of 1970?

A Well, I can't apply the term "distortions" to other companies. All I can say is that I did receive, as do other members of the industry, I did receive a report issued by the Liberty National Bank of Louisville, Kentucky, which indicates what happens to be in storage in Kentucky in the various bonded warehouses in Kentucky and it does show the distillation ages of all the whiskeys in the various warehouses by year of distillation.

Q That report that you referred to -- did I hear you correctly -- it only referred to the whiskeys that were stored in Kentucky at the time -- as of the time the report speaks?

A That's correct.

Q Were there whiskeys stored, bulk whiskeys, bourbons and straight whiskeys, were there whiskeys of that kind stored in states other than Kentucky?

A Yes, there were.

Q By Schenley?

A By Schenley and by every other distiller with the possible exception of small Kentucky distillers.

Q What knowledge did you have with respect to the age and volume of whiskeys, bulk whiskeys stored in states other than Kentucky?

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MR. SILVERMAN: If your Honor please, I will rise, because to bring back --

THE COURT: We are getting an awfully long way away from this affidavit.

MR. ODELL: Your Honor --

MR. SILVERMAN: Just a minute, Mr. Odell. Let me just voice my objection.

In the affidavit in paragraph 44, Mr. Shuman comes to some -- has an opinion with respect to the value of Schenley's assets in connection with its competitors and the ratios of inventories to sales and of accounts receivable. That is the thrust of these questions.

His conclusion is set forth in that paragraph, and in Exhibits 21 and 22 to his affidavit is the source of that information, and those come from the financial companies of the various -- the financial -- the reports of those companies.

Where are we going in terms of this examination?

THE COURT: I don't see that this is profitably getting what is stored in other states by other companies.

MR. ODELL: We do have another statement in here where Mr. Shuman refers to this Kentucky bank report and talks about the fact that Schenley has the greatest amount of whiskey, six years or older, stored in Kentucky, and he

draws a conclusion from that that reflects adversely on the earnings and -- past earnings and the future earnings of Schenley and what I'm trying to bring out here is that the whiskey stored in Kentucky is not the sum total of all whiskey stored in bulk, that a reliable conclusion of the kind that has to be drawn there must be drawn on the whiskey, the bulk whiskeys stored in all states, not just in Kentucky.

I was looking for that reference but it is one of the points I wanted to make with respect to the Shuman affidavit.

THE COURT: It would seem in order to draw that inference, you are going to have to practically have a separate trial of what was stored in all the various states for really a marginal type of inference.

MR. ODELL: Well, your Honor, I was of the opinion, at least based on my experience in this case and what I have learned about the whiskey business, that we did not need that kind of a trial and I don't know how we would ever get to that point, because it would involve direct evidence by every large distilling company in America and I was trying to establish that the question of exactly how much or approximately how much in bulk whiskeys are stored in states other than Kentucky is more or less a matter of

conjecture as to which no one person can draw any reliable conclusions.

That is the point of this question.

THE COURT: That just makes the inference that you want to draw on the final analysis all the weaker, or one on which reasonable men can differ.

MR. ODELL: It also makes the conclusion drawn by Mr. Shuman -- I was going to find it for you if I had another minute -- it also questions the reliability of Mr. Shuman's conclusion.

THE COURT: I think your foundation is laid for the argument that you want to make, in any event, is it not?

MR. ODELL: Pardon?

THE COURT: The foundation is laid for the argument that you want to make, in any event.

MR. ODELL: Well, I think that may be so, your Honor, but I would like to have it in other authority than argument from me. I was hopeful that Mr. Chernow could enlighten us on that point.

THE COURT: Can you do that in one or two questions without --

MR. ODELL: Let me try, your Honor. None of these are very easy questions to draw on. Let me see what I can do about that.

2 THE COURT: Are you possessed of any information
3 in the years 1968, 1969 or 1970, with regard to the
4 storage of -- what is this bourbon?
5 THE WITNESS: Primarily bourbon, sir.
6 THE COURT: -- in states other than Kentucky?
7 THE WITNESS: There is a federal government
8 report which indicates total gallonage stored in various
9 states around the country. It does not, however, identify
10 it by ownership or by ownership of the warehouse in which
11 it might be located.
12 The Liberty Bank, which relates only to that
13 stored in Kentucky where there is fundamentally a fair
14 proportion of the total bourbon, does identify it as to
15 ownership of the warehouse. That doesn't necessarily mean
16 that all the barrels are owned by the warehouse owner.
17 THE COURT: Does that cover all the storage
18 throughout the country?
19 THE WITNESS: The federal government report,
20 which shows it by state and in gallons, whereas the Kentucky
21 report is in barrels, presumably on the reliability of the
22 government figures, does cover all whiskey produced.
23 They do have different categories, though. It
24 is not strictly identifiable as bourbon. They categorize
25 it as whiskey, distilled under 160 proof, which technically

2 throws it into a category.

3 THE COURT: The Liberty Bank study gives the

4 owners --

5 THE WITNESS: Gives the ownership name of the

6 warehouse in which this whiskey is stored with a presumption

7 that a significant portion of what may be stored in this

8 warehouse is owned by the warehouse owner.

9 THE COURT: So even that isn't necessarily

10 reliable?

11 THE WITNESS: It is not.

12 THE COURT: The federal report has no ownership

13 information at all?

14 THE WITNESS: No, sir.

15 THE COURT: All right. Other than that, you have

16 no input whatsoever, you personally have no input whatsoever

17 on this question Mr. Odell has been raising?

18 THE WITNESS: No.

19 MR. ODELL: Thank you, your Honor.

20 BY MR. ODELL:

21 Q Let me invite your attention to the case sales

22 of Schenley and the other companies in the industry.

23 Are the number of cases of whiskey sold by

24 Schenley itself, are those a matter of secrecy and privacy

25 as far as the rest of the world is concerned, and

2 particularly your competitors, actual number of cases sold?

3 A Yes. The entire industry attempts to preserve

4 privacy as to the branded identification of the units of

5 sale.

6 Q Similarly, are the marketing profits and gross

7 profits obtained from the sale of case goods by each

8 company, a matter of the same degree of secrecy and privacy?

9 A I would have to say even more so.

10 Q Are you in a position to say or know whether, for

11 example, Schenley's marketing profit on its case goods sales

12 of bourbon are greater than, say, those profits from sales

13 realized by National Distillers?

14 A It would not be something that I would know. I

15 am not in a position to know, in direct response to your

16 question.

17 Q Similarly, I'd ask the same question with respect,

18 say, to Seagram's in brands of -- in bourbons, straights

19 and bourbons sold by Seagram's in terms of number of cases

20 sold and marketing profits on those sales as compared to

21 similar statistics of Schenley.

22 A There is no degree of accuracy of the guesstimates

23 that have to be made.

24 Q Would that similarly be true of the other

25 companies, particularly those in the business of selling

bourbons and blended whiskeys in this country, say, American Distillers?

A I would say that is the universal application.

Q It would apply in the case of everyone of your competitors and with respect to almost every brand of whiskey they sell and you sell, is that correct?

A Yes.

Q Did you give Mr. Shuman any figures that showed the number of cases sold by major types of whiskey by Schenley together with their marketing profit for the years 1968, 1969 and 1970?

A I may very well have.

Q I show you Plaintiffs' Exhibit 34 for identification and ask whether this is one of the exhibits conveying that information that you gave to Mr. Shuman.

A This appears to be an internal memo that I may very well have given to Mr. Shuman, yes.

MR. ODELL: I offer it in evidence, your Honor. Would you like to see it?

THE COURT: Do your adversaries know what it is you are offering?

MR. SILVERMAN: I would like to know the purpose of the offer.

Does it dispute something somebody said?

MR. ODELL: I think it disputes some of the things Mr. Shuman said in his affidavit concerning the profit potential, the actual profits derived by Schenley, marketing profits from its case sales.

MR. SILVERMAN: If your Honor please, I have no objection to it if you merely observe this is a document that Mr. Chernow gave to Mr. Shuman.

THE COURT: It will be received.

(Plaintiffs' Exhibt 34 for identification received in evidence.)

Q I notice this exhibit bears a date of March 31, 1971, and a legend on a small piece of paper attached to it.

Is that a legend that you prepared on or about that date?

A I may very well have.

Q At the March 31, 1971 meeting -- March 25th meeting of the board of directors, at which Mr. Shuman was present, did any discussion take place at that meeting with respect to the increased case sales and increased marketing profits of Schenley's from case sales in the year 1970 over 1969?

A I don't recall a specific discussion of increased case sales at that meeting on March 25th.

Q Do you recall any discussion by Mr. Shuman as to

2 a decrease in case sales?

3 A I recall no discussion of either an increase or

4 a decrease in the sales.

5 Q At that meeting at which Mr. Shuman was present.

6 did he express any opinion as to the possibilities or

7 probabilities that Schenley's earnings and sales would

8 improve in the future?

9 MR. SILVERMAN: Your Honor, we have had testimony

10 all morning about what Mr. Shuman said at that meeting. The

11 witness testified at length.

12 He then said that other than the matters that he

13 had testified to, he had no specific recollection, and the

14 questions this afternoon now go to did he say (a) or (b) or

15 (c).

16 I suggest that is merely duplicative of the

17 questions put this morning to which the witness has said he

18 did not have any recollection. All afternoon with respect

19 to the specifics, he has said he has no recollection.

20 THE COURT: Mr. Odell, was Mr. Chernow's

21 deposition taken?

22 MR. ODELL: Yes, sir.

23 THE COURT: Did you ask these questions on the

24 deposition?

25 MR. ODELL: I did but they did not let him

2 answer it. They did not permit me -- they did not permit
3 the witness to answer any questions that related at all to
4 anything that was contained in Mr. Shuman's affidavit.
5 Now, to make matters worse --
6 THE COURT: I am talking about what was said
7 at the meeting of March 25th, were there questions asked at
8 that deposition about his recollection of that meeting and
9 what was said?
10 MR. ODELL: Your Honor, let me explain what
11 happened. I didn't get to that in my deposition.
12 My depositon of Mr. Chernow was abruptly ter-
13 minated on short notice whereupon I made an application --
14 by the defendants -- whereupon I made an application to
15 continue his deposition and that matter was finally referred
16 to Magistrate Schreiber, who concluded that any further
17 examination of Mr. Chernow should take the form of written
18 interrogatories and while I did propound some
19 interrogatories to Mr. Chernow, I felt, and I said so at the
20 time, said so to at least one judge in an effort to review
21 that or had something to do with that determination, that
22 the only way you can get into this question properly is
23 through depositions and not through --
24 THE COURT: In any event, you did not ask him
25 before. All I am getting at is, do you have any

2 expectation here of getting any answers other than you have
3 been getting all afternoon with these questions?
4 MR. ODELL: Your Honor, based on my success to
5 date, I'd have to say absolutely no.
6 THE COURT: I see.
7 MR. ODELL: I have to be frank about it.
8 THE COURT: If it doesn't take a great of time,
9 we can go on this way but let's move it along.
10 (Continued on next page.)
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Q Mr. Chernow, are there any statistics which attempt to show the share of the market that Schenley enjoys with respect, say, to bourbons or scotch whiskey?

A We do have statistics prepared within our company with that particular focus in mind, yes.

Q Well, are there -- and those statistics in your company refer not only to your -- Schenley's share of the market in a particular type of whiskey, but the share of your competitors?

A They are estimates as they relate to what the total is and what our competitors' share of that total may be.

Q Do you know what the basis for those kinds of statistics are? What is the source of the information upon which they are based?

A Are you referring to the statistics prepared within our company?

Q Yes.

A Some of the states do provide specific information, either as to the sale of brands or the movement of cases in to the wholesaler. They are of two different qualities, though. It is almost a bit like adding oranges and apples.

There is a trade association which attempts to

calculate as reasonably as it possibly can its best judgment as to the total consumption, and, again, its best judgment as to the consumption by category of distilled spirits.

It is against that public -- I should say "public" -- industry-available general information that we internally attempt to relate our actuals as known to us in order to determine what our share of that estimated total might be, so that, in effect, while the total may be estimated by third parties, our units of depletions -- and here is a term which I might have to define, sir.

Sales are a two-type category in our industry. Shipments generally refer, or the dollar sales that are accumulated by virtue of shipments generally refer to the movement of merchandise from us, the distiller, to the wholesaler or to the control state. However, as a real practical matter, since we are primarily concerned for management and operational purposes in the movement of goods, we are primarily concerned with the movement of that merchandise from the wholesaler to the retailer, or from the control state to the actual consumer. Those we call depletions, as against case sales or case shipments.

When we take the numbers that I just described in accumulation, we would normally apply our depletions, which are as close to an actual as we can get, against our

best available total shipment or consumption figures.

Q What does that comparison -- what is the significance of the product of that comparison?

A The significance of that is that since we are interested really in the movement of units of cases by brand or by name to the point of its actual sale to a consumer, it is that type of information which is of far more interest to us than how much might have been shipped to a wholesaler, and I'm talking now in a marketing management sense.

Q Do each of the distilling companies maintain, like Schenley does, a record-keeping system on depletions?

A I am sure most of them do, in one form or another.

Q And are these figures as kept by the various distilling companies on the depletions interchanged as between distilling companies?

A They certainly are not.

Q You also talked about some industry-wide estimates made by various associations as to -- did you say consumption?

A There are estimates made as to consumption, as to apparent movement of goods, and as to billings. There are at least three varieties of shipments made.

Q Well, with respect to each of the three varieties,

what --

THE COURT: Where is this taking us?

MR. ODELL: Your Honor, I'll tell you where this is taking us. Some of Shuman's conclusions expressed in this affidavit are based on depletion figures and industry-wide figures, and I'm trying to show through Mr. --

Have I answered your question?

THE COURT: Trying to show what?

MR. ODELL: I'm trying to show that these figures that relate to competitors' sales or portions of the marked based on depletions, in comparing Schenley's operating results, if you want to call it that, with the operating results of other companies, based on these kind of statistics, are, at best, based on guesstimates.

THE COURT: And then what?

MR. ODELL: So that Mr. Shuman in his affidavit, and I didn't want to get into that, there are pages here where he is referring to the fact that Schenley's share of the market in scotches, in bourbons, in gins, in vodkas, is less than everybody else's, less than most of the other people in the industry and, therefore, its earnings are not to be given as high a value for evaluation purposes as some of its competitors. And that's the basis for some of the --

THE COURT: All you are doing is establishing his figures are subject to very uncertain factors we have just heard testified to.

How does that advance your cause at all?

MR. ODELL: It advances my cause in this respect. If Mr. Shuman's general conclusions as to value are that Schenley is not as profitable a company as the other companies, it doesn't enjoy the shares in the market for particular whiskeys as much as other companies have a higher percentage of the market, and, therefore, while some of the companies, for example --

THE COURT: Yes, but I had thought that you were going to show that the figures given him were false and misleading. All that you are doing is establishing that the figures that were given him are subject to some question because of the murkiness of the area and the inability to get good figures.

MR. ODELL: What I have shown is,your Honor, based on Exhibit 34 which I offered, which is actual sales --

THE COURT: I am getting into what we have had testimony about here. I was wondering why you were getting into this.

It doesn't seem to me this is advancing --

MR. ODELL: It isn't advancing my case?

THE COURT: Yes.

MR. ODELL: Your Honor, I feel it is because the whole basis for Mr. Shuman's low opinion of Schenley as a distilling company and the value of the stock is based on these figures that relate to Schenley's share of the market, the number of leading brands Schenley has, the fact that Schenley has higher inventories than the other companies have, older whiskeys than other companies have, and for all of those reasons he is saying that Schenley's earnings should be valued on the basis of 13 times earnings, rather than other companies whose earnings are currently being valued in the market at 20 or more times earnings.

MR. SILVERMAN: Your Honor, that's a free-wheeling figure --

THE COURT: You are dealing again with disclosure and not with judgment.

MR. SILVERMAN: And he puts it in his affidavit as his estimate, and he points out where his estimates come from.

Where is the conspiracy in this?

THE COURT: I am frank to say I don't see the value of spending the time on this.

MR. LEVIN: If your Honor please, there has

already been testimony that none of this came before the board, to the best of this witness' recollection.

THE COURT: On the limited issue of how it helps your cause to show the statistics that Shuman used are subject to an awful lot of error because of the circumstances under which they are obtained, it doesn't seem to me it advances your cause at all, and that's what you have been asking him for about five or ten minutes here, where he gets them, how he gets them, does he get them from competitors, which obviously everybody must assume the answer is "no."

MR. ODELL: My position is that Mr. Shuman in his affidavit didn't go to the actual results of operation as they were known --

THE COURT: They were given to him.

MR. ODELL: Yes, but he didn't use them and he didn't refer to them in his opinion.

THE COURT: That's not what you have been asking about. That's something again.

All right. I made myself clear.

MR. ODELL: All right, your Honor. I think I am through with this subject. I think that when there is more time and the witness is not present, I'm quite sure that I can at least demonstrate to you the basis for

this opinion.

THE COURT: That's another matter. We will get to that at a later point.

MR. ODELL: I did want to establish what I have and I have succeeded with this witness as to that.

Could we have a short recess, your Honor?

THE COURT: We will take our midafternoon recess.

(Recess)

(Continued on next page.)

2 MR. ODELL: Your Honor, I have but a few more
3 questions left for Mr. Chernow.
4 I'd like at this point to offer in evidence, the
5 Shuman affidavit that's been the subject of so much
6 discussion.
7 MR. SILVERMAN: I object, your Honor.
8 THE COURT: Yes, objection sustained.
9 MR. ODELL: Your Honor, may I ask the grounds for
10 denying --
11 THE COURT: What is the purpose of the offer?
12 Let me turn it around.
13 MR. ODELL: The purpose of the offer is to show,
14 as best as is possible under the circumstances here, what
15 were the grounds for Mr. Shuman's opinion that this stock
16 was worth only $29 a share, and to show as actual figures --
17 and some of our later witnesses, including our accountant
18 and our financial expert, will show that the important facts
19 concerning the value of this company, such as surplus cash,
20 the increased earnings, increased sales, increased marketing
21 profits of Schenley were given in some cases no consideration
22 and in other cases very slight consideration in arriving at
23 the value of the stock.
24 Secondly, to the extent that we can derive here
25 from Mr. Chernow, as a director of this company, the basis

for Mr. Shuman's opinion as to value as expressed in this affidavit was not disclosed to the board of directors.

THE COURT: At a later time in this trial and with a different foundation, some or all of that affidavit may become admissible.

At this point, I am going to sustain the objection.

MR. ODELL: Your Honor, I would take it the ground of your objection is not hearsay.

THE COURT: I'm not so sure that that may not be a ground of my objection, but my objection, nevertheless, is that I'm going to sustain it. I will sustain the objection at this point.

MR. ODELL: Your Honor, may Mr. Zulack be heard on this further?

THE COURT: No, let's go on. You have no foundation for this exhibit at this point.

I don't know anything about it except that you represent to me that it is an affidavit. I don't know what parts you want in, what parts you don't want in. I don't know what parts are admissible, what are not.

I am certainly not going to take wholesale an exhibit which you used perhaps 3 percent of that may contain all sorts of extraneous matters.

There is no foundation for this exhibit at this time. It may be at a later stage in the trial there will be a proper foundation for its admission, but I see no foundation for it at this time.

I sustain the objection.

MR. ODELL: Well, your Honor, let me just ask another question or two of Mr. Chernow.

BY MR. ODELL:

Q Mr. Odell, did Mr. Shuman -- was he hired to render a report on the fairness of the terms of this merger?

MR. SILVERMAN: Your Honor, there has been testimony to that effect.

THE COURT: That report is in, isn't it?

MR. SILVERMAN: Yes, sir.

MR. LEVIN: The letter of June 3rd, which was attached to the minutes, is already in evidence.

Q Is the letter of June 3, 1971, the entire written report of Mr. Shuman on the basis of which the board voted to approve this merger on the --

MR. SILVERMAN: Objection.

MR. LEVIN: Objection.

THE COURT: Are you trying to bring this affidavit under the umbrella that it is part of the opinion?

MR. ODELL: Your Honor, I'm trying to find out

2 what was the basis --

3 THE COURT: No, you are offering an exhibit.

4 The only questions we are involved with here have to go to

5 the foundation or admissibility of that exhibit.

6 Q Was Mr. Shuman retained for the purpose of

7 defending the fairness of the terms of this merger in the

8 case entitled David J. Green & Company against Schenley

9 Industries? Do you know?

10 A I would have to presume so.

11 THE COURT: Mr. Odell, didn't you tell me that

12 you are bringing this gentleman here?

13 MR. ODELL: I expect to bring Mr. Shuman.

14 THE COURT: Then I don't understand all of this

15 agitation over this exhibit.

16 I thought I suggested three or four times that

17 a foundation might be laid, if necessary.

18 If you are going to have the man here, you can

19 ask him an awful lot of questions. You can use the exhibit

20 in any appropriate way that as a trial lawyer you deem

21 suitable.

22 MR. ODELL: It seems to me I am entitled to find

23 out, as I tried to --

24 THE COURT: No, you are entitled to see whether

25 this exhibit is admissible as of this moment. You asked me

2 to take it in evidence. I said no. Now you are pressing it
3 upon me.
4 I say wait until you have the man here. I don't
5 understand, frankly, why we go on with this. If Mr. Shuman
6 is going to be here, let's do it then.
7 MR. ODELL: Your Honor, what I am trying to
8 establish at this point with Mr. Chernow is, what is the
9 report that Mr. Shuman rendered, is this the report he was
10 paid to render, and I'm not talking about this affidavit.
11 THE COURT: This is an affidavit in a legal
12 proceeding. It is not a report.
13 MR. ODELL: I am talking about the report dated
14 June 7th.
15 THE COURT: I know, but we are talking about that
16 affidavit.
17 Please, go on to something else, will you?
18 If you are still pressing upon me the admissibility of that
19 exhibit --
20 MR. ODELL: No, I am not pressing the
21 admissibility of this. You have ruled upon that and I am
22 not pressing on the admissibility of that.
23 I am pressing on the fact that I would like this
24 witness to tell me if this is the report, the June 7th --
25 June 3,1971 letter, if this is the report for which,

2 according to the proxy statement, Allen & Company was paid
3 $200,000 to render an opinion.
4 MR. SILVERMAN: If your Honor please, the
5 testimony thus far is clear. Mr. Shuman rendered an oral
6 report. It was followed by a letter which summarized that
7 oral report.
8 THE COURT: I understood that this morning.
9 BY MR. ODELL:
10 Q Apart from this affidavit, Mr. Chernow, and apart
11 from the June 3, 1971 report, and apart from what you have
12 testified Mr. Shuman orally discussed with the board of
13 directors as to the basis for his opinion that the terms of
14 this merger were fair and equitable, were there any other
15 documents prepared by Mr. Shuman and given to Schenley which
16 were used as a basis for the opinion that is expressed in
17 this proxy statement --
18 MR. SILVERMAN: Objection as to form.
19 THE COURT: No, I will take it.
20 Are there any other documents that you received
21 from Mr. Shuman?
22 THE WITNESS: I don't recall receipt of any other
23 documents.
24 THE COURT: All right.
25 MR. ODELL: Let me ask a few more questions, if

2 I may, with respect to the discussions that took place at
3 the March 25th board of directors meeting.
4 Q Did any discussions take place at that meeting
5 as to the use that would be made by Schenley of the proceeds
6 to be obtained from the sale of Buckingham?
7 A I don't recall such a conversation or a
8 discussion.
9 Q Did you at that meeting present to the board any
10 statements which would reflect the receipt by Schenley of
11 the proceeds of this Buckingham sale and that would show the
12 total cash and marketable securities Schenley would have on
13 hand assuming that sale was consummated?
14 A No.
15 Q And was any discussion as to that question
16 between any of the directors and you held on that question of
17 total cash and marketable securites that Schenley would have
18 on hand?
19 A Not to my best recollection.
20 Q Did any director of Schenley at the March 25,
21 1971 meeting indicate that he had any reservations about the
22 fairness of the terms of this proposed merger?
23 MR. SILVERMAN: I thought that question was --
24 MR. LEVIN: I object.
25 THE COURT: Sustained as to form.

Q Did any director at the meeting, at this March 25, 1971 meeting, state that he was opposed to this merger?

THE COURT: I think that's been answered, has it not?

MR. SILVERMAN: Yes, sir.

MR. ODELL: I'm not sure it has. I don't remember asking it.

I am talking about the 25th meeting.

THE COURT: You may be right. Go ahead.

A No.

Q Did any director of Schenley say that he would not recommend to the stockholders of Schenley that they accept or vote in favor -- strike it.

Did any director of Schenley present at that meeting say that he would not recommend that a Schenley stockholder vote in favor of this merger at the stockholders meeting?

A No.

Q Was a draft of the proxy statement reviewed at this March 25th meeting?

A Not to my best recollection, no.

Q Was it presented to the board of directors?

MR. SILVERMAN: When?

Q Was a draft of a proxy statement presented to

2 the board of directors at that meeting?

3 A Not to my best recollection, no.

4 Q At the February 25, 1971 meeting, there is a

5 reference in the resolution as follows, the resolution

6 that -- Mr. Silverman, in the minutes that I obtained from

7 Haskins & Sells of the February 25th meeting that go forward

8 from where the minutes went that you produced for my use

9 here, there is a resolution that reads as follows:

10 "Resolved that the officers of this corporation

11 be and are hereby authorized and empowered to do any and all

12 such further acts and things including, without limitation" --

13 and I am going to skip a few lines, and there is a

14 "Provided, however, that any definitive agreement of merger

15 shall first be submitted to this board of directors for

16 approval."

17 I am reading from that minute.

18 I ask whether a definite agreement of merger was

19 submitted to the board of directors of Schenley for approval?

20 A When?

21 Q At a meeting after the one of February 25th that

22 ordered that such a definitive agreement be submitted.

23 A I can only make a presumption that it was.

24 Q But you don't know?

25 A I don't recall that single specific act.

2 Q Further on in that minute, that set of minutes
3 that I have from Haskins & Sells --
4 MR. SILVERMAN: Are they in evidence? Why don't
5 we talk about them as an exhibit?
6 MR. ODELL: 64-B.
7 MR. SILVERMAN: Thank you.
8 Q 64-B, page 10, refers to a resolution shown there
9 authorizing the officers of the corporation to file with the
10 Securities and Exchange Commission, at its office in
11 Washington, preliminary copies of such notice, proxy
12 statement and form of proxy.
13 My question to you is, at this March 25th meeting
14 from which I am reading, was a draft of the proxy material
15 presented to the board?
16 MR. SILVERMAN: Will you show the witness the
17 minutes so he can refresh his recollection?
18 MR. ODELL: Sure.
19 MR. SILVERMAN: Mr. Odell, I have given Mr.
20 Chernow a more legible copy.
21 MR. ODELL: Thank you very much.
22 A Yes.
23 MR. ODELL: What was the question again?
24 (Question read.)
25 THE WITNESS: No, that is a question. My yes

there was a question to get his question.

In response to your question, I will have to read from the minutes. It says, "There was presented to the meeting" --

THE COURT: Do you have an independent recollection?

THE WITNESS: No, sir.

Q Whatever the minutes say on that subject, you will accept, won't you?

A Yes.

THE COURT: The minutes speak for themselves.

Q The plan of agreement and reorganization dated May 21, 1971, between Schenley and Glen Alden is attached to this proxy statement of May 10th. It has a "whereas" clause that reads as follows, and I'll read it with you so that you can follow me.

"Whereas, the board of directors of Glen Alden, as subsidiary, and Schenley believe that the terms and conditions of this plan and agreement of reorganization will be in the best interests of said corporation and their respective stockholders."

Referring to that "whereas" clause, did you as an officer and director of Schenley believe that this merger was in the best interests of Schenley?

2 MR. LEVIN: I object, if your Honor please --

3 MR. SILVERMAN: What is the relevance of the

4 question?

5 MR. LEVIN: -- to disclosure.

6 THE COURT: What is the relevance of the

7 question? Where are you reading from?

8 MR. ODELL: I am reading from Exhibit A, which

9 is at the back of this proxy statement.

10 THE COURT: Page what?

11 MR. ODELL: There is no page, your Honor. It

12 follows page F-33.

13 THE COURT: What is the relevance of this

14 question?

15 MR. ODELL: This proxy statement, your Honor, is

16 unusual for proxy statements heretofore, theretofore filed

17 by Schenley and thereafter filed by Glen Alden in which

18 there is no statement made in the body of the proxy

19 statement as to the purpose of the merger, the reasons for

20 it, and the nearest I can get to the purpose or reasons for

21 this merger is what I would call boiler plate language in

22 the body of this agreement that is at the back of this

23 proxy statement.

24 THE COURT: All right, I will sustain the

25 objection.

CROSS-EXAMINATION

BY MR. SILVERMAN:

Q Mr. Chernow, did you supply Mr. Shuman with all the information he asked you for?

A I did.

Q The second question is in connection with Exhibit 17, which is the May 31st balance sheet, a copy of which I would like to show the witness, and I call your attention to the item Marketable Securities, $124,530,000.

Are the proceeds of the sale of Buckingham reflected in the balance sheet under that item?

A They are.

Q Does the balance sheet show the gross proceeds from the sale of Buckingham?

A Yes.

MR. SILVERMAN: I have no further questions.

THE COURT: Anyone else on cross-examination?

MR. CANTOR: No questions.

MR. SEASONWEIN: No questions.

MR. LEVIN: I have no questions.

THE COURT: Mr. Odell, any redirect based on the cross?

MR. ODELL: No, sir.

THE COURT: Very good. You may step down.

2 (Witness excused)

3 MR. ODELL: Your Honor, I think this would be
4 a good time before calling another witness, since we have
5 about a half-hour, to clear away some of these exhibits
6 that are going to be -- that have been used already and
7 will be used in connection with witnesses that will be
8 forthcoming. I think we could save a lot of time and,
9 with your permission, I would like Mr. Zulack to handle
10 it.

11 THE COURT: I had even planned to stay tonight
12 until a quarter of 5:00, so you can count on forty-five
13 minutes worth of time.

14 MR. ZULACK: Your Honor, there are certain exhibits
15 to which I believe we have no dispute with respect to
16 Schenley, which have not been introduced, and they are
17 Exhibit 13, Schenley profit and loss balance sheet before
18 audit reclassification, dated December 31, 1968.

19 MR. SILVERMAN: No objection.

20 THE COURT: Received.

xxx 21 (Plaintiffs' Exhibit No. 13 was received in
22 evidence.)

3b 23 MR. ZULACK: Your Honor, our next offer is --
24 there is an objection, but it is a qualified objection,
25 that is, as to Exhibit 12-A, which is the Schenley 10-K

2 for 1971. There is an objection as to relevancy with
3 respect to that period after the merger. That would be
4 for the months from July to December.
5 We would like to submit it on the basis that
6 it is a fuller statement of the annual report, Exhibit
7 No. 10 already in evidence, as we need that document for
8 our expert to base certain opinions upon. We think it's
9 related to the merger in the sense it's the same year.
10 THE COURT: Is there objection to the entire
11 exhibit?
12 MR. SILVERMAN: If your Honor please, the '71
13 annual report is in. This is no more.
14 MR. LEVIN: I should like to inquire as to what
15 the expert's opinion will relate to.
16 MR. SILVERMAN: If your Honor please, before
17 pursuing that, Mr. Levin, let's do this, and we will --
18 let's come to that in due course.
19 These things are admissible or not on the issue
20 of disclosure.
21 MR. ZULACK: A companion document is item
22 Exhibit 16 which is a Schenley profit and loss statement,
23 but for the year 1971. The objection on the pretrial order
24 is it's after the period of June to December. We have '68,
25 '69 and '70. We would like to have 1971 to continue

the comparisons.

MR. SILVERMAN: Again, I assume that my friend is representing that this is relevant to the issue of disclosure and not for any other purpose.

MR. ZULACK: It is.

THE COURT: On that basis it will be received.

Plaintiffs' Exhibit 16 received in evidence.

(Plaintiffs' Exhibits Nos. 16 and 12-A were received in evidence.)

MR. ZULACK: Our next offer, your Honor, is as to Exhibit 17-A, which is the quarterly balance sheets of Schenley. The objections --

MR. LEVIN: For what period is that?

MR. ZULACK: The period is from 1968 to 1971.

MR. SILVERMAN: I don't understand the relevance of this material in light of the question of disclosure, unless it is said that we should have disclosed these quarterly balance sheets or what?

THE COURT: What do they add to our store of knowledge?

MR. ZULACK: Your Honor, I think what it adds is we have -- one of the questions on disclosure is, obviously, our issue of surplus cash.

Our accountant has had to use quarterly balance

2 sheets as well as year-end balance sheets because of
3 the strange year period which Schenley had. It had a
4 year ended August 31, '68 and then it was changed to
5 December 31, '68.
6 For some comparitive purposes it was helpful
7 for him to use quarterly balance sheets, I believe. It
8 is essentially to simplify the issues we are going to
9 present to the Court.
10 THE COURT: I'll receive them.
xxx 11 (Plaintiffs' Exhibit No. 17-A was received in
12 evidence.)
13 MR. ZULACK: Your Honor, our next offer would
14 be Exhibits -- I think it's better to treat them together
15 because there are four which are substantially alike.
16 These are inventory blue books which break down the quantity
17 of distilled spirits which Schenley had on hand during the
18 applicable periods. We believe it's relevant because one
19 of the ways in which surplus cash was accumulated was, in
20 our view, through the reduction of inventory.
21 We believe we can show this -- and also through
22 age, we can show this through these exhibits.
23 MR. SILVERMAN: Stipulated Facts 20 and 21, we
24 have the stipulation -- and 22 -- forgive me, 20 and 21
25 have the inventory records stipulated as facts, I thought.

MR. ZULACK: Your Honor, the other aspects of this are that not only does -- do these books show the amount of inventory, but they show the cost of inventory.

We have certain allegations about nonrecurring costs, and the only way we can show these nonrecurring costs is from the price allocated to each of these items in these inventory blue books.

THE COURT: I can't say that I follow that at this moment, but, in any event, these inventory blue books are kept in the regular course of business, and I take it would be admissible on that basis.

MR. SILVERMAN: Subject to the relevancy objection, your Honor.

THE COURT: Subject to the relevancy objection, I'll take it.

MR. ZULACK: Those numbers are 30, 31, 31-A, 32 and 33.

MR. SILVERMAN: Wait awhile. 30 is a summary.

Are you representing that as a blue book? I thought that --

MR. ZULACK: It's a summary in dollars. I understand them as related documents.

MR. SILVERMAN: I can understand -- I don't understand. 30 and 31. What about 32? That's the blue book

dated, or for the year January 1, '72?

MR. ZULACK: It would be through December 31, 1972.

MR. SILVERMAN: I object to that because it is well beyond --

THE COURT: This is for the year '72?

MR. SILVERMAN: That is what document 31-A apparently relates to.

THE COURT: Is there a unique relevance to this document covering a period after the --

MR. ZULACK: Your Honor --

MR. ODELL: Your Honor, the purpose of getting these documents and now using them is to show that after the date of the merger, and through December 31, 1972 at least, without going any further ahead, that certain types of Schenley's inventory, particularly Indiana bourbons and corn whiskey were reduced without being replaced, and it was part of a continuing process that started with this new management, I believe in the fall of 1968 and, certainly, by the beginning of '69. And it's part and parcel, as far as I'm concerned, of showing the results of conditions that were operative in the years immediately prior to the merger, that continued thereafter, and it's part of the basis, I might say, for an opinion as to the amount of

Schenley's surplus assets and surplus cash or surplus assets to be reduced to cash after June of '71, the merger date. That process was continued.

THE COURT: All you are going to have is the figures themselves? You will have no testimony about these figures at all?

MR. ODELL: I am. Our expert will testify about them.

THE COURT: That's the figures themselves, plus argument from them, but you have no other proof with regard to these inventory figures to --

MR. ODELL: Your Honor, we do have the testimony of Mr. Chernow with respect to this inventory in his deposition that this process of removing distortions and also using certain types of inventory without replacement continued after December 31st and continued after June of 1971, and I think there is some testimony here today that the constant aim of this company was to continue to remove distortions in inventory.

MR. SILVERMAN: I don't understand this in the context of a disclosure case with respect to a proxy statement that was issued sometime in the spring of '71 for a merger consummated in June of '71.

MR. ODELL: Your Honor, our expert will testify

as to the amount of surplus cash that Schenley had on May 31, 1971, and that that amount of surplus cash could be removed from Schenley without in any way affecting its operations, and he will also testify, based on the testimony of continued reduction of certain types of inventories that following May of 1971 and in accordance with the testimony of Mr. Chernow, there was some $26 million of Indiana bourbon and corn whiskey which was not being replaced and which was gradually going to be liquidated over a period of years at a rate of consumption per year that's shown by the consumption experience with respect to those inventories in 1969, 1970 and in the first six months of '71.

THE COURT: Then what?

MR. SILVERMAN: If your Honor please, there is a stipulated fact dealing with just this subject. 41 says the following chart shows the amount of Schenley's inventories as of the dates indicated of certain bulk whiskeys for which new production had been discontinued, and which were being phased out without replacement, and then it goes into non-Kentucky, new wood and corn whiskey from -- the year December 31, '70 and the year December 31, '71.

I don't know what more one can want with respect to a disclosure case dealing with a 1971 merger, and I, for

the life of me, don't understand what '72 has to do with that.

MR. ODELL: All '72 -- all '72 figures will show is that in '72 the rate of consumption of those whiskeys continued as they did in '70 and '71.

Now, if you are willing to stipulate now that the Indiana bourbons and the corn whiskeys were eliminated at the rate of about $6 million a year in 1972, as they were in '71 and '70, then I don't need this.

MR. SILVERMAN: You are right, if I will stipulate that which you want in, you don't need it.

I suggest to you it is not properly in this case and I therefore renew my objection --

THE COURT: Why is it in this case?

MR. ODELL: Your Honor, one of the areas of testimony of our expert, financial expert, will be --

THE COURT: No, no. What is the proof? Forget where it comes from. What is the fact that you hope to prove by this?

MR. ODELL: All I hope to prove is that the process of reducing these inventories to cash in the amounts shown in the '72 report that Mr. Silverman is objecting to actually occurred in accordance with the --

THE COURT: How do you tie that into the cause of

action?

MR. ODELL: I tie it into the cause of action in this way:

Our expert will testify that a minimum of $140 million of surplus cash was in Schenley and should have been given independent weight in valuing the worth of Schenley.

MR. SILVERMAN: That's a fairness case.

MR.ODELL: No, sir.

MR. SILVERMAN: You can argue that when your expert comes.

MR. ODELL: We will show that the removal of $140 million of cash from Schenley will in no way adversely affect its operations in the future, because additional cash will be forthcoming from -- apart from earnings, from the continued liquidation of these particular whiskeys, the $26 million worth of whiskey, so that there is no strain placed on -- there is no abnormality on the removal of at least $140 million of cash from Schenley in connection with this merger.

MR. SILVERMAN: Your Honor, the issue --

MR. ODELL: Your Honor, it's not that it's not that big a point, and I don't think it's worth getting into the protracted argument we are getting into. I would have

1 thought that -- I said all I can say in support of it.
2 I don't think the argument is worth --
3 MR. SILVERMAN: I will renew my objection on the
4 grounds that this disclosure case revolves about was
5 there a sufficient disclosure in the proxy statement that
6 a lot of money was going, cash, from Schenley to Glen
7 Alden, was that adequately disclosed.
8 The rest of this, it seems to me, is just
9 irrelevant. I therefore renew my objection to so much of
10 Exhibit 30 as relates to the period after the merger --
11 all right, for the year 1972, since that goes from '68
12 through '72. I therefore object to the '72 part of that.
13 I object to 31 -- 32, which is the inventory
14 blue book, January 1, '73.
15 I object to 33 insofar -- which is a Schenley
16 summary of inventory -- insofar as it pertains to the
17 year 1972.
18 THE COURT: I am going to reserve decision on that
19 entire offer.
20 MR. ODELL: Thank you.
21 MR. ZULACK: May we have it marked pending --
22 THE COURT: It's already marked for identification.
23 MR. ZULACK: May we --
24 THE COURT: As I understand your respective
25

2 positions, you say that this should be admitted because
3 it shows that the Schenley management knew that it would
4 have cash coming in from inventories that were not being
5 replaced?
6 MR. ODELL: That's right.
7 THE COURT: And, secure in that knowledge, it
8 was in a position to transfer upstairs $80 million having
9 gotten clearance for 115; that's what the argument amounts
10 to, and that's all that you are asking that it be received
11 for?
12 MR. ZULACK: Yes, your Honor.
13 THE COURT: Mr. Silverman says it's wholly
14 irrelevant because it's not a question of could it -- was
15 management secure in the knowledge that it could shoot
16 the money upstairs. The only question was, did they
17 say they were going to do it by saying "we are going to
18 transfer a substantial amount of funds."
19 MR. SILVERMAN: And we transferred 80. 20 came
20 back.
21 THE COURT: You transferred 80 and some 20 came
22 back and, therefore, the offer is irrelevant, in any
23 event.
24 Let me think about that.
25 MR. ODELL: Won't you at least concede that the

20 that came back went out again?

MR. SILVERMAN: I said over the next four years it dribbled back out again.

THE COURT: In any event, I understand your respective positions on this offer.

MR. ZULACK: Your Honor, may we offer and have marked those portions as to which there is no objection and reserve -- obviously, you have reserved decision on the '72.

THE COURT: You certainly may.

MR. SILVERMAN: There is objection to so much of the exhibit as relates to the year '72.

THE COURT: I can receive them excpet as to '72, which I will reserve.

xxx (Plaintiffs' Exhibit No. 30 was received in evidence.)

xxx (Plaintiffs' Exhibit No. 31 was received in evidence.)

MR. ZULACK: May I address Mr. Silverman, your Honor?

THE COURT: Sure.

MR. ZULACK: Mr. Silverman, is your objection to the entirety of 31-A before I offer it, or just those portions after --

MR. SILVERMAN: Sorry, if I said 31-A. That should have been -- I assume -- let's look at 31-A so -- is that through December 31, '71?

MR. ZULACK: It's through December 31, 1971, but it's marked as of January 1, 1972.

MR. SILVERMAN: I have no objection to that.

I have objection to the next one, which is 32.

MR. ZULACK: Fine.

xxx (Plaintiffs' Exhibit No. 31-A was received in evidence.)

MR. ZULACK: For the reocrd, we are not marking 32 in evidence.

MR. SILVERMAN: No, since the Judge has reserved on that, I think that's proper.

MR. ZULACK: Your Honor, I am handing the clerk Exhibit 33 for identification to be marked in evidence.

MR. SILVERMAN: Except for the year 1972.

MR. ZULACK: With the exceptions stated on the record.

xxx (Plaintiffs' Exhibit 33 was received in evidence.)

MR. ZULACK: Our next offer is as to Exhibits 118 and 119 which I bring up because I believe there are no objections as to those. 119, 120.

MR. SILVERMAN: Are these summaries of some of

2 the other exhibits you have put in?

3 MR. ODELL: These are summaries of the blue books

4 which were given to Mr. Gluck on the defendants' side

5 several months ago, that were prepared by our accountants,

6 and I believe it was with the understanding if they found

7 any inaccuracies in those summaries they would let us know.

8 MR. SILVERMAN: Mr. Odell, do I understand these

9 are summaries of the materials that have just been put

10 into evidence?

11 MR. ODELL: They are.

12 MR. SILVERMAN: On the theory if it's good once

13 it's better twice?

14 MR. ODELL: Not on that theory at all.

15 MR. SILVERMAN: Perhaps it might help the Judge

16 if we just had the summaries.

17 MR. ODELL: I think you need both. These

18 summaries merely show the actual consumption and the age

19 distribution of the consumption in the years covered by

20 the blue books.

21 MR. ZULACK: There is no objection to them in

22 our pretrial order. They have -- there is no objection to

23 them.

24 MR. SILVERMAN: That's because we objected to

25 the blue books. We now have the blue books admitted. It's

a little strange.

xxx (Plaintiffs' Exhibit No. 119 was received in evidence.)

xxx (Plaintiffs' Exhibit No. 120 was received in evidence.)

MR. ZULACK: We have no more offers at this time, your Honor. We thinkg we might make some at a later date.

THE COURT: We will stand in recess until 10:00 in the morning, 10:00 o'clock. We will sit from 10:00 until 1:00 o'clock tomorrow.

(Adjournment taken to October 17, 1975 at 10:00 a.m.)

MR. ODELL: There may be one more. I want to check my notes.

In the meantime, your Honor, I believe we can put the witness on from Haskins & Sells who is in charge --

MR. ZULACK: I think we are going to call a different witness.

I would like to call the representative of Shearson, Hayden, Stone.

Is he here in the courtroom?

C H A R L E S N A S T R O, called as a witness by the plaintiffs, being first duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. ZULACK:

Q Mr. Nastro, by whom are you employed?

A Shearson, Hayden, Stone.

Q What is your position?

A Vice president, associate general counsel.

Q Mr. Nastro, would you tell us whether or not Shearson, Hayden, Stone was served with a subpoena in this case?

A Yes, it was served upon me personally.

Q Was it a subpoena duces tecum?

A Yes.

Q Did that subpoena duces tecum call for the production of a report dated October 6th of October 1972, with respect to the merger of Glen Alden and the Rapid-American Corporation?

A Yes, it did.

Q Did it call for the production of that document by a person who had knowledge of the preparation of that report?

A Yes, it did.

Q Does, Shearson, Hayden, Stone have anyone available who was involved in the preparation of that report?

A The individual who prepared the report is no longer with the firm.

Q Do you know where he is?

A I do not.

Q Do you have the report with you?

A Yes, I do.

Q Do you have any knowledge whether or not Shearson, Hayden, Stone was paid for the report which it rendered to the corporation?

MR. SILVERMAN: Objection. I don't see the relevance of that. This is a 1972 report.

THE COURT: I don't even know what the report is

about.

MR. SILVERMAN: I'm not sure either.

A We were paid $150,000.

THE COURT: I will take that fact. It may or may not have relevance.

MR. ZULACK: Your Honor, on that basis, I offer the report into evidence --

THE COURT: That is not much of a basis.

MR. ZULACK: I will be delighted to argue that if I may, your Honor.

THE COURT: All you have established is that they paid $150,000 for the report and that was no foundation for putting it in evidence on this trial.

Q Do you know whether the report speaks, evaluates the Schenley stock which Glen Alden Corporation owned?

MR. SILVERMAN: Objection.

THE COURT: Sustained.

Mark it for identification for now, first.

(Plaintiffs' Exhibit 113 marked for identification.)

MR. ZULACK: Your Honor, may I be heard on this particular offer?

THE COURT: You may.

MR. ZULACK: Your Honor, I think the witness may

2 be excused because I have no more questions for the witness.

3 THE COURT: You better stay here.

4 MR. SILVERMAN: We may have some questions.

5 MR. ZULACK: Your Honor, when Mr. Riklis was on

6 the stand, I asked Mr. Riklis if, in fact, Hayden, Stone had

7 written a report evaluating the merger of Schenley and Glen

8 Alden in 1971 and after showing him a statement in the proxy

9 statement of 1972, which referred to that fact, he said, "I

10 accept that." That is on page 192 of the transcript.

11 I asked if Hayden, Stone had written a report

12 regarding the merger of Rapid and Glen Alden in 1972 and he

13 said, "I do, I accept that, too."

14 Now, the question is whether or not that is a

15 sufficient foundation for the admissibility of a report and

16 as I mentioned at that time, there are two entries.

17 One is, is that hearsay. We clearly do not have

18 the person who prepared the report here to be

19 cross-examined, but does that make any difference? We

20 contend that under Rule 801(d)(2)(d), it clearly does not and

21 that rule states --

22 THE COURT: Let me get a few underlying facts

23 squared away.

24 This report, as far as you know, for whom was it

25 prepared and why?

MR. ZULACK: It was prepared for the board of directors of Rapid-American Corporation, a defendant and party opponent in this lawsuit, and the report so says in its body that it was prepared for them.

In addition, Mr. Riklis has testified that the report was prepared for them.

MR. SILVERMAN: If your Honor please, it may not be a wholly true statement.

May I have a voir dire so we can get on the record what this document appears to be?

THE COURT: Well, obviously I'm groping for facts here and I need a lot more than I have.

MR. ZULACK: Your Honor, there is no -- I think --

THE COURT: Is this being offered because somebody who made a report that is employed by a brokerage house made certain opinion statements about something?

MR. ZULACK: No, your Honor. This report was made --

THE COURT: Just answer my question.

MR. ZULACK: No.

THE COURT: What are you offering it for?

MR. ZULACK: Your Honor, I heard that question a particular way, "Was an opinion by Shearson, Hayden, Stone generally as to the value of Schenley stock as any other

brokerage firm might evaluate a stock?

"No.

"Was Shearson, Hayden, Stone hired by Rapid-American to judge the fairness and the equitability of a merger between Glen Alden and Rapid in 1972?

"Yes, it was.

"As part of that merger, did Shearson, Hayden, Stone, or Hayden, Stone at that time have to opine that the value of the Schenley stock owned by the Glen Alden Corporation to be merged with Rapid-American was worth a certain amount?

"Yes, it did.

"And did that report track a report, which is in evidence, which was written by the same corporation, the same company in 1971?

"Yes, it did."

THE COURT: What leg up does it give you?

MR. ZULACK: Your Honor, the leg up as to relevance is that we are dealing with three corporations which are highly interrelated corporations. Rapid-American --

THE COURT: You say all this does is repeat something in an earlier report?

MR. ZULACK: It repeats it but there is a substantial difference.

2 The difference is that the report in 1971
3 attributes a substantially lower value to Schenley than the
4 report in 1972.
5 THE COURT: That custs against your position.
6 MR. ZULACK: No, it cuts in favor of our
7 position, your Honor, because we maintain that there have
8 been reports which were written for the managements of
9 these companies in 1967, 1968, 1971 and 1972. All are
10 glowing recommendations about this company except for one
11 and the only one which is a very pessimistic -- and we say
12 totally bad faith -- report is the Shuman affidavit.
13 THE COURT: I understand that.
14 MR. SILVERMAN: I thought VBWL had made a report
15 in 1971 about this merger.
16 MR.ZULACK: Your Honor --
17 MR. SILVERMAN: Which is not a question of
18 disclosure, your Honor, because the VBWL report was given to
19 the Glen Alden board and we are dealing, as I understand it,
20 with a Schenley proxy statement.
21 MR. ZULACK: Your Honor, I appreciate that the
22 board that Mr. Silverman would like to make a large
23 distinction between the Schenley board and the Glen Alden
24 board. The Schenley board had all appointees of Glen Alden.
25 Several of the directors were also members of the Glen Alden

2 board and I think it is a highly formalistic distinction
3 to make between these two companies.
4 What I'm talking about is the actual knowledge
5 that these directors of the Schenley board had, what sort of
6 knowledge was available to them in 1971, and is it all
7 probative that in 1972, another investment banker, which
8 one of the corporations, one of these Riklis corporations
9 hires, comes and says, this stock is worth a lot more money
10 when it is in their interest to do so.
11 THE COURT: Let me ask you this:
12 You are not going to have any proof, as I
13 gather, as to who the man was, the basis of the man's
14 opinion, any instructions that were given to him, any
15 materials that were furnished to him, anything that was said
16 to him in connection with the preparation of the report,
17 nothing?
18 (Continued on next page.)
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MR. ZULACK: Your Honor, absolutely none, and the reason for it is this:

On July 1, 1975, the federal rules of evidence were changed to make clear what had been a growing trend, and that is to exclude from the exceptions to the hearsay rule the question of admissions. It used to be that admissions were essentially based upon the fact that they were reliable. Now,the fact that we have this report here has nothing to do with its reliability. It has to do with the adversary process.

Our oppoents have hired somebody to say something. We can't get that person to come here. We can't pay them $150,000 to --

THE COURT: You haven't proved that fact that they hired somebody to say something.

MR. ZULACK: Yes, I have, your Honor.

THE COURT: No, you haven't.

I'm proceeding on the premises that somebody was engaged to make an evaluation.

MR. LEVIN: If your Honor please, I think there should be added to the litany --

THE COURT: If you were to have proof that this man was told to put that figure in that report, then you have somebody who was hired to say something.

MR. ZULACK: Your Honor, have I established that Shearson, Hayden,Stone was hired to make a report and this was the report?

THE COURT: I am proceeding on that assumption.

MR. SILVERMAN: Let's be a little more precise for the record.

THE COURT: Engaged to assess --

MR. SILVERMAN: Engaged --

THE COURT: -- to assess a merger.

MR. SILVERMAN: The fairness of a different merger a year after the events that we are concerned with.

MR. LEVIN: If your Honor please, I was going to say that there should be added to the litany of your unanswered questions whether or not this report ever came to the attention of Rapid-American.

MR. ZULACK: Your Honor, there are two inquiries and I think it would be helpful if we dealt with them one at a time.

The first inquiry is whether or not this is a hearsay item because we don't have a person here to testify about the contents of the report.

The second question is,whether it's hearsay or not hearsay, is this a relevant document?

Addressing myself to the first question first, if

you look at Rule 801, there are two categories of statements, and the statement is a written version, which I contend this is. There are two categories of statements which are excluded from hearsay. One category is an admission by a party-opponent. There are five types of admissions by party-opponents. One is, and the one which we urge as the basis for the admissibility of this document, is Subdivision (d). Subdivision (d) says that any time you have a statement which is a statement by a party-opponent's agent or servant concerning a matter within the scope of his agency or employment, made during the existence of the relationship, that document is admissible.

Now, the question is, what about its trustworthiness? The advisory notes clearly say that the admission, admissibility has nothing to do with trustworthiness. It has to do with the adversary system.

We put the report in; the report speaks for itself. That's our case.

Our opponents who know about the report and who know how it was made and who hired the people come in and say this report is hogwash.

MR. LEVIN: There is nothing in the record to suggest we knew about that.

THE COURT: You are shifting a little bit of the

burden of proof in this trial by that last statement.

MR. ZULACK: As to the admissibility, I am talking about.

MR. SILVERMAN: Let's talk about Mr. Zulack's reading of the statute.

Is there any evidence of agency here, or is it rather that an independent contractor was hired for an opinion, and does that make that independent contractor an agent?

MR. ZULACK: Your Honor, the language in the statute was clearly written to overcome that sort of objection. It talks about agent or servant. An agent or a servant is synonomous with an independent contractor. It does not mean "employ."

An "agent" is a broader word, the broadest word we could use in the statute.

MR. SILVERMAN: Your Honor, there are two bases.

One is the hearsay objection; the other is relevance. It seems to me that this is excludable on both of those grounds.

It is clearly an irrelevancy as to what anyone thought in 1972, a year after, as to what the value of Schenley was in the context of an evaluation of the fairness of a merger between Rapid and Glen Alden rendered, or, if

that opinion exists, given by an independent contractor in a document about which there is no evidence with respect to whether that document ever found its way into the hands of anybody.

MR. ZULACK: Your Honor, as to relevance, this is not a jury trial. This is a bench trial.

We have three reports now in evidence: One in '67, one in '68, one in '71. It seems to us that it's only fair that you have one in '72 in order to shed light on the facts of 1971.

This is not 1980 or 1940. It's one year later. The most important thing is you look at the two reports, your Honor, which we believe had bearing on the members of the board of directors of Schenley who were also members of Glen Alden. If you look at those two reports, you will see a shocking statement of how close they were.

It is a word-for-word markup of the earlier report, and to us it's shocking that an investment banker can be hired to say the same, with the same words, come to a different conclusion.

MR. SILVERMAN: A year later.

MR. ZULACK: That is something --

MR. SILVERMAN: If your Honor please, where is the disclosure problem?

THE COURT: I'm going to exclude the exhibit on the ground of inadequate foundation, and I do not believe that it's relevant or that it is an admission within the terms of this statute. I acknowledge that the statute seems to have language that might appear to cover it, but I do not conclude that it necessarily does.

MR. ZULACK: Your Honor, may I make an offer of proof without stating -- I have given my reasons --

THE COURT: You really have.

MR. ZULACK: Just so it's marked for identification.

THE COURT: It's marked for identification.

I assume you have made your offer of proof because you have argued fully and well on this issue. I think the record is made.

xxx (Plaintiffs' Exhibit No. 113 was marked for identification.)

THE COURT: Any cross-examination?

MR. SILVERMAN: No, sir.

THE COURT: All right.

(Witness excused)

MR. ODELL: Your Honor, may I call the representative of Haskins & Sells who was responsible for supervising the audit of Glen Alden.

THE COURT: Please come up.

ROBERT J. GUMMER, called as a witness by the plaintiffs, being first duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. ODELL:

Q Mr. Gummer, you are associated with Haskins & Sells in what capacity?

A I'm a partner in the firm of Haskins & Sells.

Q How long have you been a partner?

A Since 1971.

Q As a partner, did you have any responsibility for supervising the audit of Glen Alden for the period ended December 31, 1970?

A Could you repeat that, please?

THE COURT: Read it back.

(Question read)

A Yes. I was not a partner at that time.

Q When did you become a partner?

A In June of 1971.

Q Prior to that time, what function did you perform with respect to the audit of Glen Alden for the year ended 1970?

A I was the manager on Rapid-American Corporation, the parent company, as well as another subsidiary, and had

overall responsibility with the partner responsible for Rapid-American, had overall responsibility for all units of Rapid-American Corporation at that time.

Q Including Glen Alden?

A Yes.

Q Is it fair to say that you supervised the audit, then, of both Rapid-American and Glen Alden for the year ended December 31, 1970 with respect to Glen Alden and for the fiscal year ending January 31, 1971 for Rapid-American, as it was then known?

A I was part of the supervisory team for those years, yes.

Q You were served with a subpoena here which requested you to produce all studies, appraisals, opinions and other written material prepared or received by Haskins & Sells relating to the nonamortization by Glen Alden of (a) the excess of unallocated costs of investment over equity in the net assets of Schenley.

Have you produced -- do you have with you any such papers?

A No, we have no papers with representations of that nature that were given to us by representatives of Glen Alden, I think is the way you phrased the question.

Q The second item that you were requested to produce

pursuant to this subpoena is written material of the same kind I described with respect to (a), the following written material designated as 1-B in this exhibit to the subpoena, Schenley franchises to import whiskey, liquors and other distilled spirits by brand name and dollar amount.

Did you bring with you any papers in response to that item of the subpoena?

A We received no papers from representatives of Schenley with respect to those matters.

Q You are now speaking with respect to -- I am now asking you whether Glen Alden received such papers, not whether --

MR. SILVERMAN: Objection, your Honor. I understand the question to be did Glen Alden receive --

THE COURT: That's the question he is putting now.

MR. SILVERMAN: If this witness knows or had them.

THE COURT: I don't know what the witness' answer is. I assume the answer is "no," because he didn't bring any papers.

THE WITNESS: That is correct.

Q Are there such papers in existence?

A Your question indicated did we receive anything from Glen Alden or Schenley that they would have received

concerning these matters, and the answer is "no," we did not. We have no such papers.

Q Let me ask you this:

Did Glen Alden receive any papers from Glen Alden's management concerning the excess of unallocated costs of investment over equity in the net assets of Schenley as that amount -- as that category of account was reflected in the Glen Alden financial statements that were audited by Haskins & Sells?

MR. SILVERMAN: If the witness understands the question, I have no objection, but I did not understand it.

A You are asking me if Glen Alden received something from Glen Alden with respect to these matters?

Q Yes.

A I can't respond to that. I don't know whether Glen Alden received something from Glen Alden. It's a Glen Alden matter.

MR. ODELL: Your Honor, I think a fair reading of this subpoena, the exhibit here -- in the first place, the subpoena --

THE COURT: Let me see the subpoena, Mr. Odell.

MR. ODELL: Oh, sir. I'm sorry. I ask you to look at the first page and the exhibit attached to it.

THE COURT: Mr. Gummer, you have been in possession

of a copy of this subpoena which we will mark as Plaintiffs' Exhibit 146 for identification. You have been in possession of a copy of this.

Have you studied it?

THE WITNESS: Yes, I have, your Honor.

THE COURT: When did you get it?

THE WITNESS: I believe the subpoena was received by one of my partners, I think it was early in September, if I recall, and I received it the following Monday or Tuesday.

THE COURT: You have had it for something over a month?

THE WITNESS: Yes, your Honor.

THE COURT: You have read it carefully to ascertain what it calls for?

THE WITNESS: Yes, I did.

THE COURT: Did you have any of the items that are asked for by that subpoena?

THE WITNESS: No, we don't. We made a search of our papers and we have no such items.

THE COURT: All right.

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(Plaintiffs' Exhibit No. 146 was marked for identification.)

THE COURT: Mr. Odell, if you want to inquire as to the efforts to search, and so on and so forth, you are certainly at liberty to do so.

MR. ODELL: I intend to, but I want to go to the second item of the subpoena.

Q Item 2 of the subpoena calls for all letters of representation and requests therefor which were given on behalf of Glen Alden and Schenley to Haskins & Sells for each of the calendar years 1968 through 1971 relating to (a) the nonamortization of excess of unallocated costs of investment and Schenley franchises described in Paragraph 1 above.

Do you have with you any letters of --

THE COURT: He doesn't have anything, Mr. Odell. He has answered that. He doesn't have anything. He didn't bring anything with him. He says he didn't find anything that's asked for in the subpoena, so the only inquiry --

MR. ODELL: I thought he was addressing yourself --

THE COURT: I asked him if he looked at the subpoena, studied it, and brought anything in response to it.

The only inquiry open is what is the good faith

of his efforts and what did he do.

MR. ZULACK: I think it was a problem of hearing.

MR. ODELL: I am terribly sorry, your Honor.

THE COURT: I am sorry. I thought you had understood the import of my question. I am sorry.

Q Would you tell us what search you made of the records of Haskins & Sells to determine whether or not the papers described in this subpoena were in the files of Haskins & Sells?

A Yes. I instructed my people under my supervision to review the work papers for the years in question to determine whether there was any representation that would have been received during those years, representations as you described in the subpoena, and they reported they made a full search and found nothing with respect to those matters.

Q Were there any letters of representation of any kind received from the management of Glen Alden?

A Not to my knowledge.

Q Let me finish the question.

Were there any letters of representation received from the management of Glen Alden by Haskins & Sells in connection with its audits for the years ended December 31, 1969, '70?

A What type of representations are you referring to?

Q Concerning the value of the assets of Glen Alden.

A No.

Q Did your search also include such records as might be in the files of Rapid-American relating to this subject matter that is requested by this subpoena?

A When you say "files of Rapid-American," are you speaking of the files of Haskins & Sells with regard to Rapid-American?

Q Yes.

A Yes. We looked through that, too, and there are no representations there.

Q I'm going to show you the notes to the audited report of Glen Alden for the year ended December 30, 1970 and 1969, note (d), entitled Intangibles and Francises, as shown on Page F-13 of Exhibit 1 in evidence.

A Yes, sir.

Q Did you participate in the preparation of any portion of note (d)?

A I did not participate directly with respect to note (d), no.

Q Did you supervise the conduct of the audit of Glen Alden insofar as it related to the content of note (d)?

A Yes.

Q Would you tell me whether, in connection with the preparation of the content of note (d), you or anyone else associated with Haskins & Sells made any judgment or determination as to the value of the Schenley common stock owned by Glen Alden at December 31, 1970?

A No, we would not have made that judgment particularly.

Q Are you able to say whether that would be a judgment that fell within the auditing responsibilities of Haskins & Sells?

A Well, of course, the determination of value of a stock, as you described it, would be a difficult thing for an accountant to do solely.

Certainly, one element that might be considered at a given point in time might be the market value of the stock with respect to that footnote, but that would be simply one matter among many.

Q Apart from market value, did you make any other inquiries concerning the value of Schenley for the purpose of this note?

MR. SILVERMAN: I object because it assumes he did make an evaluation when he said he did not.

THE COURT: I'll sustain the objection on the

grounds of form.

Where is this footnote, by the way?

MR. ODELL: F-13, your Honor.

THE COURT: Thank you very much.

MR. SILVERMAN: At the top of that page.

MR. ODELL: I'll withdraw that question, your Honor, and rephrase it.

Q To your knowledge, did Haskins & Sells make any study or determination of the value of Schenley as a company in connection with its audit of Glen Alden for the year ended December 31, 1970?

A We would not have made a study as to the value of Schenley in connection with preparing our report on the financial statements of Glen Alden.

Q Did Haskins & Sells make any study or investigation as to whether any diminution in the value of Schenley's shares owned by Glen Alden had occurred by December 31, 1970?

MR. SILVERMAN: I am puzzled by the formulation of the question in terms of the value of the value of Schenley shares.

Where does that appear?

THE COURT: Let me hear the question back.

(Question read)

THE COURT: I overruled the objection.

Can you answer?

A We would have looked at many things to indicate whether there was any permanent diminution in value or impairment in value, and would have tried to determine whether there was any permanent impairment and, absent that, we would have concluded, as the footnote concludes, that there is no permanent impairment.

Q "Impairment," you say? How about diminution in value?

A As long as it's permanent, it must be a permanent impairment or permanent diminution.

Q You had come to the conclusion there had been no such --

A We concluded no event had taken place which would indicate to us there was any permanent impairment of that investment.

Q I am now talking about the sentence that reads, "These net acquisition costs have been recognized by the management of Glen Alden as being similar in nature to intangibles which have not declined in value since acquisition."

Would you tell me what was the basis for the statement --

MR. ODELL: Strike the question.

Q Would you tell me whether or not inquiry was made by you or other members of the audit team as to whether or not -- as to what the management of Glen Alden had recognized with respect to whether or not these intangibles declined in value since acquisition?

A You are asking me did we make any inquiries of representatives of Glen Alden --

Q Yes. Let me just perhaps make myself a little clearer.

This note talks about these net acquisition costs have been recognized by the management of Glen Alden. Now, that note was written by Haskins & Sells, wasn't it?

A No. It was not. That note was written by officials of Glen Alden Corporation. It is their financial statement.

Q As auditors, you merely verify that that note was an accurate statement?

A We indicate in our opinion that it presents fairly in accordance with generally accepted accounting principles the matter in question.

Q What do generally accepted accounting principles require you to do when you are reviewing a financial statement of a company in relation to its statement that it has recognized that the value of these intangibles have

not declined in value since acquisition?

A First of all, the accounting principles require that where excess costs are generated in an acquisition of the type described, they should be carried at original cost until so long as an event occurs which would indicate that there is some permanent diminution or decline in the carrying value of that asset, but until that event occurs it should be carried at cost.

We would have inquired as to whether such event had occurred, either through the company officials, or would have made certain judgments in our own audit of Schenley at the same time since we had visited various locations, all of which would have led us to conclude that no event had occurred which would require amortization or writedown of that investment.

THE COURT: I am not an accountant, but let me see if I can put this:

Assuming that Glen Alden pays a premium for Schenley stock over the market, the total purchase price represents what Glen Alden feels that corporation is worth, that that stock is worth to them,or they wouldn't have laid it out; right?

THE WITNESS: That's correct.

THE COURT: Therefore, as long as what they bought

remains in roughly the same form as when they bought it, as an accountant you would carry it at what they paid for it because it still is what they bought and was worth to them what they were prepared to pay for it, obviously; right?

THE WITNESS: Yes.

For an acquisition that occurred at that time.

THE COURT: Even though the market may be lower at some point, reflecting somebody else's judgment as to what it might be worth at that time; right?

THE WITNESS: That's correct.

THE COURT: If they bought, among other things, three distilling plants and one distilling plant burned to the ground, uninsured for argument's sake, then is the value of what they bought diminished by that event?

THE WITNESS: It may be diminished, yes.

THE COURT: At that point something comes into play which has changed the essential asset that they bought and requires you to take that into account in how you carried the asset?

THE WITNESS: That's correct.

THE COURT: All right, I understand.

Q Are there any other inquiries, other than the --

THE COURT: The whole idea is if they are paying that much money for it it is an assignment by them of that

value to it and nothing has occurred to change that.

THE WITNESS: That's correct.

THE COURT: Okay.

I'm sorry, Mr. Odell, go ahead.

Q Let me ask, with respect to this sentence in note (d), "Accordingly, at the respective dates of acquisition, the management of Glen Alden adopted the policy of not amortizing these excess purchase costs so long as there is no diminution in the value of the related investment," is it true here, as you said with respect to the previous sentence, that that sentence was prepared by the management of Glen Alden?

A That is correct.

Q Again, you made whatever inquiries that we will get into to satisfy yourself that there was a reasonable basis for what is here referred to as the policy of Glen Alden of not amortizing these excess purchase costs?

A That is correct.

Q Apart from acts of God that would destroy -- let's talk first about acts of God that would destroy a plant.

Why would that fact require some consideration of whether or not amortization of the intangibles should begin?

A Well, if that were the only plant, for example, and that were destroyed as an act of God, then the company would not be able to manufacture the product which it intends to sell, and therefore wouldn't be able to earn any money, and the possible investment could be impaired, which would require either writedown -- more likely writedown than amortization of that investment.

THE COURT: You have to recognize it?

THE WITNESS: That's correct.

Q Was the history of the earnings of the company in the year which is the subject of audit, as well as those that preceded the audit,a factor that Haskins & Sells would take into consideration in reviewing the judgment of the management that no decline in value had occurred?

A It is one of the factors that would be considered, yes.

Q Would the balance sheet of the related investment, Schenley, be a factor that you, as auditors, would look at in weighing, in determining whether the judgment of the management of Glen Alden was reasonable in that respect?

A Yes, we would have examined -- we would have looked at the balance sheet as one of the factors.

Q Would the amount of Schenley's liquid assets, cash and marketable securities, be a factor in your overall

evaluation of the management's judgment as expressed in this footnote -- in this note?

A Anything reflected on the balance sheet that might be indicative of an event requiring a permanent impairment would be a matter we would look at.

Q So that would it be fair to say that, based on your review of this note as prepared by management, you looked at the earnings of Schenley in the year 1970 and in the preceding years, you looked at the balance sheets of Schenley for those years preceding 1970, and you could find nothing with respect to either earnings or balance sheet items that would cause you or auditors -- you as auditors to raise any question concerning the judgment of the management of Glen Alden as it's expressed in this particular footnote -- note that we have been dealing with?

A We would have seen nothing that would indicate that there was any indication of a permanent impairment at that point, yes.

Q At Page F-2 of this same proxy statement, there is the opinion of the independent certified public accountant, Haskins & Sells, which is dated March 12, 1971.

Would you look at that, please?

MR. ODELL: Your Honor, did I give you the page? The page was F-2 of the same sequence.

Q Would you tell me if that page does set forth the opinion of Haskins & Sells and the date as of which it was rendered? Is that correct?

A Yes, it does.

Q And it also refers that certain information in notes (k) and (m) to the financial statements being as of a later date.

Could you tell me with respect to note (m) by looking at note (m) of this financial statement, as of when, as of what later date -- what is the later date that is referred to there?

A Note (m) you are talking about, of the Glen Alden financial statements?

Q Right.

Do you have enough light?

A I believe I do.

Without a detailed reading of the note, but it would refer to any matter which occurred after March 12, 1971.

It may well be the last item. I'm really not certain.

Q Well, may I help you just a little bit, so we can move along?

A Sure.

Q Note (m), the next-to-the-last paragraph on

Page F-18, your Honor, refers to a reorganization.

A Yes.

Q So that now I'm asking you, as of what time did you learn of the reorganization as it is incorporated in that note (m) and referred to in your certificate? Sometime before May 10th, I guess, because that's the date of the proxy statement.

A Well, we would have learned in the ordinary course of events at the time that any public announcement of this reorganization was made. I assume that day is somewhere in the document.

Q You were aware at the time of this certificate that Schenley had entered into an agreement for the sale of Buckingham; is that correct?

A I believe that is one of the subsequent events that is also covered in that note, yes.

Q I believe that may be note (k) that's referred to. Let me see.

Yes, on May 10th, that's the reference contained in (k).

In determining whether this note (d) that's been the subject of your testimony so far required any revision or further consideration by you as auditors, did you consider the fact that Schenley had sold Buckingham and would, after

December 31st -- after the date of sale, lose the earnings which it had enjoyed from Buckingham for many years before then?

A That would have been one of the considerations made.

Q But you knew of that fact in connection with -- at the time of your audit and at the time of your certificate; is that correct?

A At the time of the double date referred to in the certificate, yes.

Q And did you regard the loss of income -- first, can you tell me what, as you understood it or knew it, what was the income of Buckingham at that time for the year 1970?

A You mean Buckingham's net income?

Q Yes.

A I don't recall that.

Q Would you accept what is stated in this proxy statement to be approximately what its income was? I will ask you to look at Page 24 of this proxy statement, which states that Buckingham's income was $8,710,168 in the year 1970, and $9,057,344, and relate those earnings figures to the total earnings of Schenley that is shown on Page 22 of this same proxy statement, which for 1970 was, as I read

this, a total of $27,000,000 for 1970,and $27,182,579 for the year 1970 and $25,262,886 for 1969.

Relating those earnings of Buckingham to the total earnings of Schenley for '69 and '70, was it the opinion of Haskins & Sells that the loss of income that would come from the sale of Schenley was not -- Buckingham, was not an event of such consequence as to require any modification or any reservation in your certification of management's financial statements for 1970?

A For 1970?

(Continued on next page)

Q Yes.

A Yes, because the event had not occurred in 1970.

Q But you knew the event was going to occur shortly thereafter, is that right?

A At the time of our initial expression of an opinion on the financial statements of Glen Alden, the event had not occurred. The sale took place sometime much later than that, I believe in May when our original opinion was in February or something like that.

So that the event occurred after our initial expression of an opinion. The double-dating, really, gives effect to the reference of a disclosure of a subsequent sale.

Q We will get to the finer points of that but let me ask you one question:

Where you know and recognize that a sale is going to take place like this one, isn't the imminence of that sale or the likelihood of that sale to be considered by you in rendering your opinion as certified public accountants here?

A If the event occurs subsequent to the date of the financial statements and prior to our initial rendition of the opinion, we would give effect to such an event if it had occurred.

In this particular case, we had originally expressed an opinion on those financial statements, I believe in February, whatever the date is in here. The event itself occurred at a date much later than February and the double-dating here really refers to the disclosure of the subsequent event.

We would not for that type of event adjust the financial statements on which we have already expressed an opinion. It would be an event that would have taken place in the year in which the event took place, which would have been the year ended December 31, 1971.

Q If I understand you correctly, if the sale had taken place by February 25th or as of a later date, as you referred to in your opinion with respect to the note, if the sale had occurred by that time, you would have to reflect that sale and consider that sale in connection with your certification of the financial statements as prepared by the management of this company?

A We would have had to consider that if it occurred prior to the date of our opinion, yes.

Q Let me ask you, had it occurred prior to the date of that opinion, would you then have made any adjustments or in terms of the opinion you rendered or the notes to the financial statements that you found reasonable?

MR. SILVERMAN: I object to the form.

THE COURT: Sustained.

Q Assuming the sale had occurred by February 25th, we will say, what changes would have been required of you in the opinion that you rendered and in the notes that you approved of -- management's notes as they appear in this financial statement?

A Your Honor, I can't deal with the opinion unless I know how the accounting was.

But if the accounting for the transaction as it was subsequently accounted for, there was a gain on the transaction from the sale of Buckingham by Schenley, that gain in the Glen Alden financial statements was used to reduced the excess cost, the assets that we are talking about.

I believe it was a substantial amount, somewhere in the neighborhood of $60 million. And that was recorded sometime during the year ended December 31, 1971 in the accounts of Glen Alden, so that event was really recognized as a reduction of that excess cost in that year.

Q A reduction in the amount of, you say, $60 million?

A Somewhere in that neighborhood.

Now, if you are asking me, with the same facts had this transaction occurred prior to the rendition of our

opinion would that same accounting have been made, we would have said yes, you have have reduced the excess cost to recognize that and if they had done that, then we would have expressed an opinion unchanged.

You asked me the accounting as well as what our impact on the opinion was.

Q In terms of the reduction of the intangible here as it is relfected on the Glen Alden balance sheet, would you explain to the Court, please, the various steps involved.

Let's accept your figure of some $60 million by which the intangible was reduced, and the cash and marketable securities of Glen Alden were increased by an amount even greater than the amount by which the intangible had been reduced as a result of this sale of Buckingham, is that correct?

A The cash and marketable securities were on the books of Schenley, not Glen Alden.

Q No, but as reflected in the consolidated statement of Glen Alden, which is what we are talking about here.

A My answer is yes, they would have been reflected in the assets of Glen Alden. That is what I was answering.

Q Would that amount of $60 million, and I assume --

let's assume that that was the amount because the 1971 statements will show and so will the footnotes, and I don't want to take the time to go into that in detail.

Would the reduction of the intangible by $60 million reflect the total diminution that had occurred in the value of Schenley by reason of the sale of Buckingham?

A It wouldn't necessarily reflect the total diminution, no. It would be a measurement of the permanent impairment and, therefore, a need for a write-down since Schenley sold a major asset and, as you indicated, the income stream would no longer be available to Schenley from that asset directly.

Q What I am concerned about here, and I am confused about it, Schenley receives $120 million from the sale of Buckingham and accounting-wise, you reduce an intangible by roughly $60 million and you are saying that that is a sufficient recognition of whatever loss of income that came from the sale of this investment, is that correct?

A I'm really --

THE COURT: Diminution in value.

A I said it is an indication of a permanent diminution and, therefore, a reduction of excess cost.

Q I'm going to show you the Glen Alden 10-K for

the year ended December 31, 1971, Note (d), on page F-11 of the 10-K, and ask whether in connection with your audit for the year 1971 -- now at that time you had become a partner of Haskins & Sells, is that correct?

A That's correct.

Q And you were still the man in charge of supervising this audit?

A I was responsible for the audit of Rapid-American Corporation, the parent company, and had people in my firm reporting to me who conducted that audit.

Q And in connection with that audit, you had occasion to review Note (d) to the financial statement for the year ended December 31, 1971?

A Yes.

MR. SILVERMAN: Mr. Odell, what page are we on?

MR. ODELL: F-11 of the 10-K.

MR. SILVERMAN: Of the 10-K for what year?

MR. ODELL: 1971.

I'm sorry, I have the wrong one. I'm sorry. I'm terribly sorry. I thought I had the 1971 10-K, but I had the 1970. Excuse me for taking up your time unnecessarily. I apologize.

Q I think this is the same note in the annual report and I would like the Court to see the same note.

Now, at the end of 1971 and after the sale of Buckingham had taken place and you had made what you said was the adjustment to the intangible which reduced the intangible from $85,583,000 at the end of 1970 to $68,448,000 at the end of 1971, as shown in this note with respect to Schenley, did you go through the same reviewing process with respect to management's preparation of this Note (d) to determine whether there was a reasonable basis for the content of that note as prepared by management?

MR. SILVERMAN: May I hear the beginning of that question again, sir?

THE COURT: You may.

(Question read.)

MR. SILVERMAN: The question implies that that reduction was made solely by reason of the Buckingham transaction and I do not believe that there is a sufficient factual predicate for that assumption.

THE COURT: Maybe you better ask that question of this witness as to whether he knows the components that went into that reduction.

MR. ODELL: All right.

Q What were the components that went into the reduction of the intangible as it related to Schenley in the amount of $85,583,000 in 1970 to $68,448,000 in 1971, as

stated in this footnote?

A Well, I think in reading the footnote again to refresh my memory, that it describes several of the transactions that are effected on it. I believe in the third paragraph it talks about RKO Stanley Warner Theatres.

It says, "The net proceeds of such sale closely approximated the carrying value of the asset sold after consideration of related credits and included intangibles."

That may have been part of the transactions. The Buckingham transaction was certainly one, and I believe there was another transaction involving Schenley where part of its minority interest was acquired which created an increased excess cost.

So there were a number of transactions. I believe they were the principal ones.

Q Well, in any event, did you go through at the end of 1971 the same review of the earnings statements, the balance sheets and the same material that you had referred to with respect to your review of this note for the year 1970, to determine that there was a reasonable basis for management's decision not to amortize the intangible?

A We would have done that, yes.

Q Now, this note for 1971, and I will take the liberty of saying subject to your acceptance, the same note

appears with respect to 1970, also contains a note that reads -- contains a sentence which reads as follows:

"Franchises consist of Schenley contracts to import whiskeys, liquors and other distilled spirits which in the opinion of management have continuing value and, accordingly, are not being amortized."

Do you know with respect to what brands of whiskey or spirits this note refers?

A I don't know all of them, no. It would relate to many of their, all of their existing franchises.

Q Would it include the franchise that Schenley had to distribute Dewars Scotch?

A It would, I'm sure, relate to that.

Q And what was the length of that franchise?

A The franchise, although I believe is a short term franchise is renewable yearly at the option, I believe, of Schenley, and has been renewed every year.

Q Is it at the option of Schenley only?

A I'm not certain about that.

Q Would you accept the description of that franchise as contained in this proxy statement, the length of it and its renewability and at whose option?

A Yes.

Q Well, the proxy statement reads -- May 10th --

2 at page 45:

3 "Dewars White Label Scotch Whiskey has been

4 distributed under contracts which have been renewed from

5 time to time since 1936 and the latest of which extends to

6 April 1973."

7 MR. ODELL: I can show you that contract if

8 you like. It is attached to the Shuman affidavit, your

9 Honor. Would you like to see the contract?

10 THE WITNESS: I don't know.

11 Q Would you accept that the contract was a

12 three-year contract and could be terminated by either party?

13 MR. SILVERMAN: Your Honor, we will concede the

14 description of the contract in the proxy statement.

15 MR. ODELL: Pardon me?

16 MR. SILVERMAN: We will concede the description

17 of that contract as it appears in the proxy statement.

18 MR. ODELL: I would hope you would do that.

19 MR. SILVERMAN: Then I don't understand what you

20 are going to.

21 MR. ODELL: I am going to the Shuman affidavit

22 which contains a copy of the contract and says it is a

23 three-year contract.

24 MR. SILVERMAN: There is no question pending --

25 MR. ODELL: Do you concede that the Dewars

license was a three-year license?

MR. SILVERMAN: Yes, three-year license.

MR. ODELL: Mr. Silverman, would you also concede that the $50 million of franchise value that is referred to here in the notes and in the financial statement of ~~Schenley~~ GA as an asset, $50 million attributable to franchises, refers almost entirely to the Dewars' license?

MR. SILVERMAN: I will accept the $50 million figure if you eliminate value from your question. It is the figure that appears in the financials which is attributable almost largely to or almost exclusively to the franchise involving Schenley's distributorship of Dewars.

MR. ODELL: Thank you.

Q In connection with your review of the Note (d) here in 1970 and in 1971 as it relates to these franchises, what review did you make to determine whether or not management's opinion, as stated in this note, that the franchises have continuing value and, accordingly, are not being amortized? What review did you make or investigation to determine the reasonableness of management's opinion with respect to that $50 million franchise value?

A Well, our representatives at Glen Alden would have made the same essential review that was done for the

2 excess costs that we discussed earlier; in other words,
3 geared to the fact that any event occurred which would
4 indicate that that asset should be reduced in value or
5 amortized.
6 Q Would the fact that it was a three-year license
7 require any amortization?
8 A Not at that time and not based on the facts
9 that -- although a three-year license, it had been a
10 franchise which I believe the proxy statement states was in
11 effect since 1963 and has been renewed ever since.
12 Q And that provided the basis for your finding this
13 particular portion of management's financial statement note
14 reasonable and in order by the standards of your profession?
15 MR. SILVERMAN: Objection, your Honor. I think
16 the testimony was, no event had occurred which required
17 the --
18 THE COURT: Sustained.
19 Mr. Odell, what conclusion do you wish me to
20 draw from this footnote as to the Dewars franchise in the
21 10-K? What conclusion are you seeking to have me draw from
22 the fact that you are eliciting about Dewars?
23 MR. ODELL: Well, your Honor, both the Hayden,
24 Stone opinion in 1971 and the Shuman opinion refers to the
25 fact that Schenley only has a three-year franchise for

2 Dewars and, therefore, the value of Schenley as a company,
3 since a large part or a large segment of its profits come
4 from Dewars is to be given a lesser value because it might
5 lose that franchise and a big share of its business.
6 THE COURT: I understand, all right.
7 MR. ODELL: Your Honor, I had a more substantial
8 and a more pervasive reason for going into this whole subject
9 if you would like me to tell you.
10 THE COURT: No. You go ahead.
11 MR. ODELL: May I?
12 THE COURT: Go ahead with your inquiry. You
13 satisfied my inquiry.
14 MR. ODELL: All right, sir. Thank you.
15 Is this a good time to take a recess?
16 MR. ZULACK: Yes, it is, your Honor.
17 (Recess)
18 (Continued on next page.)
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MR. ODELL: I have just one or two more questions of the witness, your Honor.

BY MR. ODELL:

Q Sir, I think you mentioned in the course of your testimony you saw the public announcement of the proposed merger between Glen Alden and Schenley, is that correct?

A Yes.

Q Would you accept that that public announcement occurred on February 25, 1971?

A If that was the fact, yes.

Q In connection with your certification of the Glen Alden financial statements for 1971 -- 1970, I'm sorry, which occurred on March 12, 1971, did you after learning of that public announcement examine the minutes of Glen Alden as they referred to this proposed merger between Schenley and Glen Alden, that is, the minutes prior to March 12, 1971, to start with?

A I did not examine them personally but we would have examined the minutes up to date of the subsequent events, the footnote that is referred to in our opinion in the ordinary course.

Q Did you or the people working under your supervision examine the minutes of Schenley for February 25, 1971, the minutes that led to the announcement of the merger?

A May I see the Schenley opinion that would have been examined through the date of the opinion on Schenley?

It would have been through February 25, 1971, and prossibly later with respect to the matter referred to in Note 9.

MR. ODELL: Your Honor, the witness is referring to page F-19 of the proxy statement in issue here and if you will just give me a minute, I'd like to look at Note 9 again.

Note 9, your Honor, refers to the sale of Buckingham as well as the proposed reorganization between Glen Alden and Schenley.

Q Did the announcement of the merger, the examination of the minutes of those two companies, as you described in your last answer, cause you or any other partner of Haskins & Sells to review at all the notes of Schenley's or Glen Alden's financial statements for the year ended December 31, 1970?

A Did the minutes cause us to review the notes?

Q Yes.

A We would have reviewed the notes to insure that appropriate disclosure had been given to the transactions you referred to.

Q I am speaking of the Note (d) which refers to

2 intangibles on the balance sheet of Glen Alden.

3 A It would not -- those events would not have

4 required modification of those notes.

5 Q Do you mind explaining why it wouldn't?

6 A Yes, because the transactions that you referred

7 to took place after the date of our initial expression of an

8 opinion on Glen Alden and, therefore, would have been

9 events that are subsequent events and I think the matters

10 as disclosed in the proxy statement are labeled "subsequent

11 events," so we would have had simply to assure that the

12 disclosure of those transactions was in the document.

13 But it would not have required a change in the

14 language of those notes -- of the Note (d) that you are

15 referring to.

16 Q You were familiar with the fact that Glen Alden

17 owned approximately 88 percent of the common stock of

18 Schenley at December 31, 1970, right?

19 A Yes.

20 Q And that, therefore, the events that were

21 scheduled to take place after February 25th with respect to

22 this merger, because of that voting power of Schenley, had

23 a strong likelihood of occurring?

24 A Well, it may have had a strong likelihood of

25 occurring but they had not in fact been consummated.

2 Q That is the test, as far as you are concerned, as
3 an accountant?
4 A What test?
5 Q That the event had to occur before you could take
6 it into account in reviewing the notes to the financial
7 statement of management.
8 A An event should occur to give effect in the
9 financial statements, yes.
10 Q The announcement itself was not regarded as an
11 event, in other words?
12 A Only from the standpoint that the announcement
13 would require disclosure in the document of the forthcoming
14 event.
15 Q In your review for the year 1971, did you or
16 any member of your staff have occasion to see an affidavit
17 of Stanley S. Shuman, dated June 7, 1971, that related to
18 the terms of this merger between Glen Alden and Schenley?
19 A I personally saw no such affidavit and I don't
20 really know whether others in my organization did.
21 Q In connection with your review of Note (d) for
22 1971, did you make any inquiry as to what the value was of
23 the Schenley common shares for the purpose of that 1971
24 merger?
25 You can answer that yes or no, if possible.

A We would not make an inquiry as to the value of the Schenley shares for purposes of that footnote. We would simply make inquiries as to whether any event had occurred which would indicate that there should be any change in the company's policy with respect to the excess cost referred to in the footnote.

MR. ODELL: Thank you very much. I'm finished with the witness, your Honor.

MR. SILVERMAN: With your Honor's consent, Mr. Gluck will cross-examine very briefly.

CROSS-EXAMINATION

BY MR. GLUCK:

Q Could you tell us under what accounting principle or rule, the treatment of intangibles is governed?

A Yes, it was then governed under Accounting Research Bulletin 43, I believe it is Chapter 5.

Q Mr. Gummer, referring to Footnote (d), do you know for how long that footnote, in substance, not in exact numbers, was found in the Glen Alden financial statements?

A It was in the Glen Alden financial statements for sometime, going back to ever since I have been involved on the Rapid-American engagement, which goes back to January 31 of 1967 -- 1968. It was in those financials at that point and I believe in there prior to that.

Q So it was in the financial statements prior to the time that Glen Alden had acquired any interest in Schenley?

A I believe so, yes.

Q I would like to go back for a moment to how an intangible is originally set up because I think I, at least, got a little confused by some of the testimony.

This sort of intangible is created when one company makes an acquisition of a substantial portion or the entire portion of another company, correct?

A That's correct.

Q It is called purchase accounting?

A That's correct.

Q Now, in setting up this footnote, does it make any difference if the acquiring company, in this case Glen Alden, pays more than, less than or the same as the market price of stock it acquires?

A No.

Q Market price is not relevant in setting up this footnote?

A That's correct.

Q Let me assume for a moment that Schenley had a book value of 100. That would be book value as expressed on Schenley's books of account?

2 A Yes.

3 Q And that the cost to Glen Alden was 200.

4 A Yes.

5 Q Is the difference between 100 and 200 the

6 intangible?

7 A Yes, it ordinarily would be, yes.

8 Q So would it be fair to say that the two

9 elements you look at in setting up the intangible is the

10 cost to Glen Alden and the book value of Schenley as

11 reflected on Schenley's books?

12 A The difference I would set up would be the

13 difference between the cost to Glen Alden, and the book

14 value and net assets value on the Schenley financial

15 statements ordinarily, yes.

16 Q When this intangible is set up, is it relevant,

17 do you make any inquiries as to what management of Glen

18 Alden thought their acquisition was worth?

19 A No. It would -e the cost, the basic figure would

20 be the cost that they paid for it.

21 Q So for accounting purposes and for purposes of

22 this intangible, the only relevant factor is cost?

23 A Yes.

24 Q Mr, Gummer, is market price or a decline in

25 market price an event that would require amortization or a

2 write-off of this intangible?

3 A Not necessarily in and of itself, no.

4 Q You are familiar with the language of this

5 footnote, aren't you?

6 A Yes.

7 Q Would you say it is common phraseology for

8 footnotes of this type?

9 A It is very common.

10 Q I want to show you page 26 of the proxy

11 statement.

12 MR. SILVERMAN: That is Exhibit 1?

13 MR. GLUCK: Yes.

14 Q I ask you if the notes on that page describe the

15 accounting treatment with respect to the intangible that

16 resulted from the sale of Buckingham and the Glen Alden-

17 Schenley merger.

18 A Yes, they do, as if those transactions occurred

19 as of December 31, 1970.

20 Q That is a pro forma?

21 A That is a pro forma balance sheet that we are

22 looking at, yes.

23 Q Do you recall if you reviewed that pro forma?

24 A We would have reviewed that, yes.

25 Q At or about the time the proxy statement was sent

2 out?

3 A Yes.

4 Q Let me see if I understand the two parts of this

5 correctly.

6 Am I correct that the sale of Buckingham led to

7 a reduction of approximately three-quarters of the

8 intnagible that was then on Glen Alden's books with regard

9 to Schenley?

10 A It would have been -- yes, about three-quarters.

11 Q You learned in 1971 of the terms of the proposed

12 Glen Alden-Schenley merger, did you not?

13 A Yes.

14 Q Do you recall that the price being paid to

15 Schenley common stockholders had a value of approximately

16 $29 a share?

17 A I heard that used, yes.

18 Q Was that an event that required a write-off or

19 amortization of the intangible?

20 A The payment of $29 to the minority common

21 interests, that would not require a write-down of the

22 intangible.

23 Q Isn't it a fact that the consummation of the

24 merger caused an increase in the intangible in Glen Alden's

25 books?

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I am now referring to Note 2 on page 26.

A Yes, it did.

Q Mr. Gummer, just one more question.

In your opinion, did Footnote (d) as it appears on page F-13 of this proxy statement that is in the 1970 financial statements of Glen Alden, did that give proper effect to the accounting rules under ARB 43, Chapter 5?

A Yes, it did.

MR. GLUCK: I have no further questions.

THE COURT: Mr. Odell, you may have redirect examination at this point, if you wish it.

MR. ODELL: I do. Just a question or two.

REDIRECT EXAMINATION

BY MR. ODELL:

Q With respect to this pro forma of Schenley on page 26, did you prepare it?

A I did not prepare it.

Q Did you audit it?

A No, I did not. We would have reviewed it but we would not have expressed an opinion on it.

Q You expressed no opinion on its accuracy at all, is that correct?

A That's correct.

2 Q Would it have been proper to express an opinion
3 by an accountant on a pro forma statement?
4 A It varies. Sometimes an accountant may be asked
5 to express an opinion simply to the effect that he has
6 checked the compilation of the -- reviewed and checked the
7 compilation of the pro formas and found it to be properly
8 compiled, or words to that effect.
9 Q But, in any event, you did not prepare an opinion
10 or give an opinion to that effect --
11 A We were not requested to do so.
12 Q As I look at this pro forma -- your Honor, do
13 you have it in front of you?
14 THE COURT: Yes.
15 Q What was the event that caused, under Note 2,
16 the second from the last column at the right-hand side of
17 that page -- I guess I better show it to you.
18 What was the event that caused an increase in
19 intangibles here of $38,457,000?
20 A I believe the $38 million arose from the
21 Schenley or Glen Alden's acquisition of the minority
22 interest in Schenley.
23 Q Do you know how much of that $38 million --
24 first, would you tell me how the $38 million was computed
25 in relation to the amounts of which the minority interests

were reflected on the books of Glen Alden prior to the 1971 merger?

THE WITNESS: Could you repeat the question, please.

THE COURT: Read it back, please.

(Question read.)

THE COURT: Let's start again, shall we?

MR. ODELL: I think we should, your Honor.

Q Would you explain the method by which the $38,457,000 increase in intangibles was computed?

A It would be determined by the difference, as the difference between what Glen Alden paid for the minority interest of Schenley, the excess of what they paid for the minority interest over the minority interest share in the net assets of Schenley at the date of acquisition.

THE COURT: The book value attributable to those shares?

THE WITNESS: That's correct.

Q Can you tell me from looking at the Glen Alden balance sheet that you have in that proxy statement, what was the book value of the $1.40 preferred on the books of Glen Alden?

A What was the book value of the $1.40 preferred?

Q Yes.

A On the books of Glen Alden?

Q Yes.

A Just for my clarification, the $1.40 preferred being the shares --

Q That were held by the --

A By the minority interest?

Q Right.

MR. SILVERMAN: I don't understand --

A I don't know if I understand.

Q I will rephrase my question.

At what value was the outstanding $1.40 convertible preferred stock of Schenley reflected on the books of Glen Alden?

A I would have to go back to the footnotes, if I may.

Q Yes, I asked you to look at the statement and I will give you the 10-K, if you like. It might help you even more.

A Well, it would be on Glen Alden's books, the carrying value of that Schenley preferred stock that you referred to would have been in the minority interest, which is a total number of $42.8 million reflected in Note (a) to the Glen Alden financials.

I don't know offhand the exact breakdown as to

what amount of that would have been related to the preferred.

Q In the course of your responsibilities with respect to Glen Alden, did you have a responsibility for the preparation of the financials to the 10-K, the annual report filed with the SEC of Glen Alden for the year ended December 31, 1971?

A No. The financial statements would be prepared by the company. We would simply, in connection with our audit, express an opinion on those financial statements.

Q But did you have any responsibility for the preparation of the financial material in the 10-K, especially that which referred to your report?

A Again, we don't prepare it. We have to express an opinion on it.

Q You see it?

A We do see it, yes.

Q And you did see the 10-K of Glen Alden for the year ended December 31, 1971, and the schedules that relate to the 10-K that are included within the 10-K?

A Yes.

Q All right, sir, and would you accept whatever the 1971 10-K shows with respect to the value at which -- the value at which the $1.40 convertible preferred and the

2 Schenley common stock held by the minority, the amounts of
3 which were reflected on the books of --
4 A I would accept that the 10-K would reflect the
5 amounts at which it is carried on Glen Alden's books, yes.
6 MR. ODELL: Your Honor, may I, so we can save
7 some time, offer in evidence the 1971 10-K of Glen Alden?
8 It is one of our exhibits.
9 MR. SILVERMAN: Is there a specific page you
10 are referring to?
11 MR. ODELL: No, there are a number of schedules.
12 They are frankly quite complicated for me to wade through.
13 They relate to the plus and minuses of the investment
14 account of Glen Alden.
15 MR. SILVERMAN: I have no objection.
16 THE COURT: All right, received. This is
17 Exhibit 114 for identification?
18 MR. ZULACK: Right.
19 (Plaintiffs' Exhibit 114 for identification
20 received in evidence.)
21 Q Was the creation of this additional intangible
22 of $38,457,000 an event within the meaning of ARB 43?
23 A You mean an event that would require a write-down
24 of that intangible?
25 Q Either a write-down or permit a write-up.

A Well, it is reflected in the pro forma as an increase in the excess cost. It would be a transaction that could under these facts create excess costs, yes.

Q And there is no doubt in your mind that in the arithmetic that led to the intangibles on Glen Alden's books going from that $85 million figure in 1970 to 68, that there was a plus there of the $38,457,000, is that correct?

A I don't know that the actual amounts in the end result but, yes, there was a plus and a minus, yes.

Q And that itself was the creation of a new intangible, wasn't it?

A It was the creation of an intangible, yes.

Q Was it a new one or an old one?

A It was a transaction that occurred at the same time as the sale of Buckingham, which was a reduction of the intangible. I believe it related in part to the initial acquisition of Schenley as well.

Q In what manner would you say, pray tell me, the sale of Buckingham created a new intangible?

A I didn't say that.

Q You said it was connected with the sale of Buckingham, didn't you?

MR. SILVERMAN: If your Honor please, may I object to this.

Now this goes into 1971 financials, that is, as of year end 1971, and the question of the amortization at that time, nothing to do with any of the financials found in this proxy statement which speak to December 31, 1970.

MR. ODELL: May I say something, your Honor?

I really find this type of objection out of order because it is telling the witness something, not me or the Court or anybody else. I had that problem once before and I did not make mention of it, but I do now.

THE COURT: I will overrule the objection.

MR. ODELL: What is the question?

(Question read.)

A I did not mean to imply that. I was saying that within those pro formas, the events, I believe, occurred almost simultaneously. I did not mean that there was a connection.

Q So the creationof that intangible had no connection with the sale of Buckingham, did it? It only arose because there was a merger?

A That intangible arose because of a merger, yes.

Q And with the creation of that new intangible, was that intangible amortized on the books of Glen Alden between June 17, 1971 and year end?

MR. SILVERMAN: Objection.

THE COURT: Sustained.

Where does this get us now?

MR. ODELL: Where it gets us is as follows, your Honor:

After this ARB 33, or whatever that bulletin is, and another ruling of the Accounting Principles Board provided that with respect to intangibles created after, I believe, October 30, 1970, regardless of what they were, even -- in other words, if Schenley was acquired by Glen Alden, we'll say on January 1, 1971, that intangible would have to be amortized over a specified period not to exceed 40 years.

I'm asking this witness whether the intanbible created by this merger of some $38 million was the subject of amortization by Glen Alden.

THE COURT: Then what? Even so, if this is after the date of the proxy statement, what difference does it make whether it was or it was not?

MR. ODELL: Your Honor, as I see this, it reflects on the whole process of bookkeeping and accounting that is involved here and I would say that in terms of disclosure and our disclosure allegations, it has no relevance to that.

It has relevance only to the accounting methods

followed by Glen Alden after June of 1971 and before the end of 1971.

THE COURT: Is this sort of an attack upon the credibility of the accounting methods at an earlier time?

MR. ODELL: No. It is not, sir.

THE COURT: I'll sustain the objection.

MR. ODELL: I have no further questions of the witness.

THE COURT: I gather you may step down. Thank you very much.

(Witness excused.)

MR. ODELL: Your Honor, I have Mr. Gardner, who is the plaintiffs' accountant and depending upon your pleasure and convenience -- Mr. Gardner is my next witness.

THE COURT: Good, call him.

MR. ODELL: I'd like to break at a convenient point with Mr. Gardner because there is a certain continuity to this examination which will take us much beyond one o'clock. We are only going to one o'clock from what you told us yesterday.

THE COURT: Let us gain as much as we can.

MR. ODELL: I will try to cover as much of the boiler plate and introductory stuff as I can.

MR. SILVERMAN: Your Honor, I understood White,

1 lzesb

2 Weld was supposed to be here today.

3 MR. ZULACK: Your Honor, I told Mr. Gluck

4 around 9:30 this morning we did not intend to call White,

5 Weld. We decided last night we were not going to call

6 White, Weld.

7 THE COURT: I see.

8 Mr. Gardner, please.

9 J O S E P H H. G A R D N E R, called as a

10 witness by the plaintiffs, being first duly

11 sworn, testified as follows:

12 DIRECT EXAMINATION

13 BY MR. ODELL:

14 Q Mr. Gardner, you are an accountant and licensed --

15 certified as such by the State of New York?

16 A I am a certified public accountant in the State

17 of New York.

18 Q When were you certified?

19. A October 1953.

20 Q Since that time, have you practiced the

21 profession of accountancy?

22 A Yes, I have been practicing as an accountant

23 since that date; as an employee previously and as a partner

24 for the last 20 years.

25 Q What is the name of your firm?

A The name of the firm is Gardner, Waschler, Freeman & Company.

Q Were you, Mr. Gardner, retained by me on behalf of the plaintiffs in this case to perform some form of review of the financial statements of Schenley?

A Yes, I was engaged to do that and other things.

Q Were you engaged as well to review the financial statements of Glen Alden?

A Yes.

Q Were you engaged to review the work papers of Haskins & Sells?

A Well, review may be a wrong word. I examined the work papers of Haskins & Sells for the accounting periods from December 30, 1968 to December 31, 1971.

Q Did you examine the accounting papers of Haskins & Sells with respect to Schenley for that period?

A Yes. That was primarily with Schenley, I'm sorry.

Q Did you examine any work papers of Arthur Andersen & Company, who audited the financial statements of Schenley for the years August 31, 1967 and August 31, 1968?

A Yes. I reviewed the work papers -- I examined the work papers of Arthur Andersen in reference to the years ending August 31, 1967-August 31, 1966, and some interim

THE WITNESS: These are the only things I have read yet that are involved. I'm sorry.

THE COURT: Mr. Odell, let's go. You were prepared to identify a statement. Let's go forward, please.

Q Did you, at my request, prepare this schedule entitled "Schenley Industries, Inc. cash,cash equivalent in marketable securities,"covering the period from August 31, 1967 through December 31, 1971?

A Yes, I did.

MR. ODELL: Gentlemen, do you have a copy of that?

THE COURT: Have you given it an identification number?

MR. ODELL: I would like to, your Honor, if I may.

May we identify this as Plaintiffs' Exhibit 147.

(Plaintiffs' Exhibit No. 147 was marked for identification.)

MR. ODELL: Mr. Silverman, I am handing the Court a copy of 147.

MR. SILVERMAN: May I just look at it?

MR. ODELL: Sure.

Your Honor, may I hand you a copy of 147 for identification.

Mr. Silverman, I'm giving Mr. Gardner a copy of

147 and I'll ask Mr. Gardner to explain briefly what that exhibit purports to demonstrate.

THE WITNESS: This exhibit was prepared from certain information given to me in reference to various statements of Schenley's.

Q Excuse me, Mr. Gardner.

Are the sources of this material stated at the bottom of the exhibit?

A Yes, they are.

Q Go ahead.

A In these exhibits, I have listed the cash, certificate of deposits, marketable securities, and the carrying value for the Glen Alden debentures when they are on the books of Schenley in the consolidated statement.

From those I deducted the amounts that were carried on the Buckingham Corporation's own set of books or statements, and arrived at a net cash or equivalent that was available to Schenley for the operation of their business, of Schenley's business, exclusive of Buckingham.

MR. SILVERMAN: If your Honor please, I understand this is a summary, purports to be a summary of material that is in the record.

THE COURT: I assume so.

MR. SILVERMAN: I, however, am informed that at

least two sources are not correct, and that is Exhibit 66 and 122.

MR. ZULACK: As to Exhibit 66, that was an oversight. There was no objection to that exhibit.

MR. SILVERMAN: What is it?

MR. ZULACK: Buckingham financial statements, 1968, four months ended April 3, 1971, and according to our correspondence, you had no objection to it.

MR. SILVERMAN: I am not objecting to its going in. I think it should be in.

MR. ZULACK: 122 is a Haskins & Sells work paper, analytical review, September 30, 1969 and September 30, 1968.

MR. SILVERMAN: May we see 122?

MR. ZULACK: Yes.

MR. SILVERMAN: I don't understand what 122 is being offered for, or what it has to do with the schedule which --

MR. ODELL: I have no objection to your asking Mr. Gardner, if that's your question.

THE WITNESS: Can I answer the question?

MR. ODELL: Wait.

THE WITNESS: Sorry, your Honor.

THE COURT: Are you offering 122?

5 lzmch Gardner-direct

MR. ODELL: I'm going to offer 122 as well as 66.

THE COURT: 66 has already been received. Without objection?

xxx (Plaintiffs' Exhibit No. 66 was received in evidence.)

MR. ODELL: 122, your Honor -- 122 is, first, a work paper of Hasking & Sells which has attached to it internal -- which has attached to it financial statements prepared by Schenley for the year ended September 30, 1969 and compares the balance sheet and income statement of Schenley for the nine months ended September 30, 1969 and for the same period in 1968.

MR. SILVERMAN: I can't read the first page of this.

MR. ODELL: I'm trying to tell you that the portion of 122 for identification, about ten pages of which deals with -- are work papers of Haskins & Sells, are not referred to whatsoever in Mr. Gardner's exhibit. What is are the balance sheets of Schenley and the income statements of Schenley for the nine months ended September 30, 1969, prepared in '68. And I am prepared to divorce the two and offer only the financials.

THE COURT: Any objection?

MR. SILVERMAN: I have no objection to putting in

those portions or that portion of Exhibit 122 which consists of the statements of consolidated profit and loss, consolidated balance sheet, consolidated statement of retained earnings and capital surplus, which appears in the latter part of the exhibit, and is not the Haskins & Sells notes, and I take it that's all my friend is offering.

MR. ODELL: That's right.

THE COURT: That will be received.

MR. SILVERMAN: All of this material is already in evidence through other exhibits.

MR. ODELL: I don't think so, but it's not in this form.

(Plaintiffs' Exhibit No. 122 was received in evidence.)

Q Mr. Gardner, do you have any --

A To be honest with you, I have lost where we were.

What I said was I had prepared this information from this various data, and what I had done was list the cash certificates of deposit, marketable securities, the Glen Alden debentures as carried in the consolidated statement of Schenley Industries, and subtracted from that the items that were carried on the books of Buckingham Corporation, to determine the net cash available, net cash or equivalent, in our opinion, available to Schenley for

the operation of Schenley's business without regard to Buckingham.

MR. SILVERMAN: If your Honor please, I will object to so much of the witness' testimony as makes the conclusions which are incorporated in the words "net cash available to Schenley."

If my friend wants it for the mathematical computation, that is, the consolidated statement less Buckingham's figures, that is fine.

It is the appellation which I believe is --

THE COURT: This is opinion evidence on his part.

MR. SILVERMAN: Then I suggest, sir, that there is no basis for an exhibit which purports to be a summary of other documents which permits of the label on that exhibit, "Net cash or equivalent available to Schenley."

THE COURT: What you are, in effect, saying is there is no basis in any Schenley exhibit for that designation.

MR. SILVERMAN: Precisely.

THE COURT: Therefore, the only basis on which that can come in on this exhibit is as a statement of opinion of this witness which is to be weighed as one of the factors in this case.

MR. SILVERMAN: Yes, sir, but I have heard no testimony about that, short of the conclusion, and all that

has been offered now is a document, and I have no objection to the document absent that conclusory language, which is for your Honor to find.

THE COURT: At this stage of the game, I will sustain that objection.

I will assume that Mr. Odell will have the witness testify as to what that language means, and we will then have a basis on which that language can be admitted and considered by me.

MR. ODELL: Your Honor, may I ask that you reserve decision on that subject to connection which can be made in the absence of Mr. Gardner?

THE COURT: No, I don't think it can be made in the absence of Mr. Gardner, because he is needed to identify what that figure stands for.

Q Mr. Gardner, tell us, if you will, what was the basis in this Exhibit 147 for your deducting from the consolidated figures of Schenley that appear at the top of that exhibit those that relate to Buckingham Corporation?

A Well, prior to the -- during the period of August 31, 1967 to December 31, '70 referred to in this -- shown on this page, Buckingham was not 100 percent-owned subsidiary of Schenley, and, as such, the assets of Buckingham were only included in the Schenley financial statement from the

point of view of consolidation.

The assets of Buckingham were not used in the operation of Schenley's business other than Buckingham's, so, therefore, the cash that is deducted by going through this mathematical calculation to determine the cash or equivalent that was available to Schenley for its operation of its business, since in all the work papers I examined of Haskins & Sells and the papers I saw, in no place did Schenley use any of the assets of Buckingham for anything but Buckingham's business.

MR. SILVERMAN: Your Honor, I'll move to strike this testimony if it is to be used as an expert opinion as to what cash is usable or is excess in an operating business.

I suggest that this witness is unqualified to make that determination. The expertise which he claims is not of that nature. Therefore, I consider his opinion on that subject to be incompetent in this trial.

MR. ODELL: May I say a word, your Honor, if you like?

THE COURT: Well, that gets you back again to whether those seven words should be on this statement.

MR. SILVERMAN: It does, your Honor, and indeed I thought it was the purpose of the question, and since that

* * * * * * * * * * *

THE COURT: Go ahead.

Q Go ahead, Mr. Gardner.

A That's really what I have done on this statement, this exhibit.

MR. SILVERMAN: I move to strike the witness' testimony on this subject because I consider it --

THE COURT: Without foundation.

Sustained.

In this state of the record, it is stricken.

MR. ODELL: As I understand your objection, Mr. Silverman, to the nomenclature used, "Net cash or equivalent available to Schenley," is that the nomenclature you are objecting to?

MR. SILVERMAN: The appellation is -- otherwise it's just a mathematical computation, and if it will help, put it in.

MR. ODELL: Before I offer it, your Honor, may I say one thing:

The proxy statements that have been offered in evidence here, dealing with the relationship of Buckingham to Schenley, contain statements to the effect that under the license agreement under which Buckingham sells the Cutty Sark whiskey, it is required to have a separate board of directors, a separate management, and required to be

operated independently of Schenley.

Now, that's the basis for this exhibit which subtracts from the total consolidated cash and marketable securities those belonging to Buckingham.

THE COURT: There is no disagreement on that.

MR. SILVERMAN: There is no disagreement on that whatsoever.

MR. SILVERMAN: That's a mathematical calculation that we are not objecting to.

MR. ODELL: I don't understand your objection to the title.

THE COURT: That certain legal conclusions flow from a factual statement implicit in that statement which Mr. Silverman doesn't believe has been established on this record.

I agree with him.

MR. ODELL: May I offer the exhibit subject to the -- what are the words here you would like deleted, Mr. Silverman, that you find have a --

MR. SILVERMAN: I thought htey had already been deleted.

MR. ODELL: Pardon me.

MR. SILVERMAN: The words are "Net cash or equivalent available to Schenley."

THE COURT: At this point those words are out.

MR. ODELL: I offer those words in evidence.

THE COURT: Without those words.

MR. ODELL: Without those words.

THE COURT: They will be received without those words.

(Plaintiffs' Exhibit No. 147 was received in evidence.)

MR. ODELL: My next exhibit, which I will ask the court reporter to mark as 148 for identification, is an exhibit entitled "Schenley Industries, Inc., change in cash, certificates of deposit."

That's the first line of the exhibit.

I give you a copy of it, Mr. Silverman, so you can find your own copy. I ask the court reporter, with the Court's permission, to mark it as 148.

(Plaintiffs' Exhibit No. 148 was marked for identification.)

Q Mr. Gardner --

MR. SILVERMAN: May I have one question on voir dire?

THE COURT: Sure.

VOIR DIRE EXAMINATION

BY MR. SILVERMAN:

Q Mr. Gardner, is this anything but a comparison between two balance sheets, May 31, '68 and May 31, '71? Is it a strict line-by-line comparison?

A Substantially that.

There may have been one or two minor assets lumped together in order to make it less confusing. Where it says on Page 2, "other current liabilities," there might have been two liabilities lumped together.

I don't recall, but, basically, exactly what you said.

Q Are they both computed without Buckingham, or is the '68 with Buckingham and is the '71 without Buckingham?

A The footnote at the bottom says we excluded the cash or equivalent of $33,558,000 owned by Buckingham Corporation at May 31, '68.

Q And also, this says at May 31, '71. Am I reading your footnote incorrectly?

A The footnote? The footnote is incorrect. It's a typographical error.

It should say May 31, '68.

MR. SILVERMAN: Has that been changed on the exhibit offered to the Court?

MR. ODELL: We will.

Q Do I understand that cash is then added back in on Page 2?

A That's correct.

MR. SILVERMAN: It says what it says, and I can't comment on that.

(Plaintiffs' Exhibit No. 148 was received in evidence.)

MR. ODELL: Your Honor, may I show it to you.

DIRECT EXAMINATION CONTINUED

BY MR. ODELL:

Q I ask you to summarize briefly what the first page of this exhibit purports to demonstrate, and what the second page purports to demonstrate.

A The first page of the exhibit is a calculation of the change in the cash position of Schenley from May 31, 1968 to May 31, 1971, and the statement of the reduction of overall debt, long and short term, during -- from the same two dates, from May 31, '68 to May 31, '71. That's the first page.

The two items are totaled together to give a total change in cash and equivalent and debt, to give a total improvement of $215,588,000.

Q Mr. Gardner, would you go to the second page, and

I would suggest you speak a little slower so that the court reporter doesn't have to break his neck to pick up your words.

A Sorry.

According to Page 1, the total improvement of cash or equivalent was $215,588,000. $215,588,000 between May 21, '68 and May 31, 1971.

Beneath that, I listed the sources of this improvement. The first source referred to page 1 was $33,588,000 that had been on the Buckingham -- been owned by Buckingham Corporation at May 31, '68. There was an increase in retained earnings between these two dates of $109,951,000.

There were various changes in the net worth section of the capital surplus preferred stock and common stock, which I lumped together as to one figure which showed a change of $5,548,000.

There was a decrease in accounts receivable of $22,541,000.

There was a decrease in inventory of $38,415,000.

There was a conversion of good will on the books of Schenley to cash of $16,414,000.

There was a tax savings on the inventory writeoff of $9 million.

A total of $235,457,000.

There were other uses of cash which used up in total $19,869,000 on the net improvement of $215,588,000.

Q With respect to the figure of $109,951,000 as the increase in retained earnings, does that $109,951,000 include the gain from the sale of Buckingham?

A Yes. It was reflected on the May 31st statement.

Q And does it include the gain from the sale of the domestic wine business?

A Yes.

Q Would you explain the conversion of good will to cash on Schenley's books of $16,414,000,telling us exactly what that conversion consisted of?

A Well, it's rather simple, actually.

Good will is the same as any other asset. It's part of the basis of the cost of the asset. In this case, this is primarily Buckingham, the -- Schenley's good will in the ownership of Buckingham, its share in the ownership of Buckingham.

When Buckingham was sold, this amount was treated as a cost part of the sale and an equivalent amount of cash or other assets were received, and this was removed from the balance sheet at that time.

MR. ODELL: Your Honor, I hope I am not imposing

on you. I always have problems in understanding, and I wanted to make sure there was no lack of understanding here.

Q This $16,414,000 was the conversion of what was previously treated as a good will item on the balance sheet of Schenley attributable to its excess cost of investment, of acquisition over its investment in Buckingham; is that correct?

A Yes.

Q And on the sale of Buckingham, that good will item of $16,414,000 became converted into cash on the books of Buckingham --

A No, on the books of Schenley.

Q On the books of Schenley, either cash or marketable securities.

A Whatever Schenley did with the proceeds of the sale.

MR. ODELL: I offer Exhibit 148.

THE COURT: It's in evidence.

MR. SILVERMAN: If your Honor please, I am sorry. There is a voir dire and I may have an objection to a portion of this exhibit. If I may for a moment.

THE COURT: Go ahead.

VOIR DIRE EXAMINATION

BY MR. SILVERMAN:

Q Mr. Gardner, Page 2 says "sources of increase in cash."

Is this a sources of increase in cash schedule as you know it as an accountant?

A You have to read further, sir. It says "sources of increase in cash or equivalents and debt reduction."

Q Let me examine a little bit -- let me ask you:

The $109 million increase, $71 million is attributed to Buckingham, is that correct, so that --

A I don't recall the exact figures, but approximately that, yes.

Q Would you look at Page 43 of the proxy statement if there is any question?

A I have no question, Mr. Silverman.

Q So you don't question that?

A No.

Q With respect to the decrease in accounts receivable, do you know how much of that is Buckingham's portion?

A No, I can't answer that.

Q Would you accept that it's about 5.5 million?

A At this moment I can't answer you, other than to accept what you say.

Q Well, this is a sources of increase in cash or equivalents and debt reduction; isn't that right?

A That's correct.

Q And I am now trying to ascertain what the source --

MR. ODELL: Your Honor, is this cross-examination or voir dire?

THE COURT: No, this is voir dire on the admissibility of the document --

MR. ODELL: Which has already been admitted.

THE COURT: I have given Mr. Silverman liberty to inquire as it if had not been admitted.

THE WITNESS: I am sorry, Mr. Silverman. I didn't hear your last question.

MR. SILVERMAN: Would you read it, please?

(Question read)

Q I am trying to ascertain what the source of the $22,541,000 figure is.

Is a portion of that the Buckingham -- attributable to Buckingham?

A Based on your statement to me, yes.

Q Do you know?

A Not from this document, no.

Q Do you know from your work as an expert?

A Yes.

Q Then what do you know with respect to --

A I know that Buckingham's accounts receivable were included in the May 31, 1968 statement.

By May 31, 1971, Buckingham had been sold, so it would not be in the May 31, '71 statement.

Q You don't really disagree that it's about 5 or 5-1/2 --

A Not at all.

MR. ODELL: Your Honor, I think we can determine the exact figure if, in fact, it is. I don't like Mr. Gardner, without having access to the records, going along with, apparently with Mr. Silverman, but whatever the figure is -- whatever the fiture is, we will have no difference in agreeing.

Q I notice a figure of $38,415,000, which is a decrease in inventory.

A That's correct.

Q What is the source of that decrease? How much of that is attributable to Buckingham?

A I'd have to look further. I can't answer from this document.

Q Do you know whether, indeed, for the fifteen months prior to 1971 there had been any decrease in inventory in Schenley?

Q Do you know?

A At this moment? I would have to look at the record. I couldn't answer that to my knowledge.

Q You have stated, I believe, that the $16 million figure of conversion of good will to cash is a Buckingham item, or attributable --

A Attributable to Buckingham, or possibly some small amount to one of the other assets sold.

Q But substantially?

A Substantially Buckingham.

Q The tax saving on inventory writeoff, isn't the source of that all Buckingham?

A I don't quite understand the question on that. I am sorry, Mr. Silverman.

Q The figure that you put in --

A Yes, sir.

Q -- as tax saving on inventory writeoff, would you tell me if there is a portion of your decrease in inventory figure attributable to Buckingham; is not the last item also partly attributable to Buckingham?

A The tax savings on the inventory writeoff either could have come as it was treated by Haskins & Sells at the end of the year from the extraordinary gain, or it could have gone against the tax savings on the other

operations of Schenley.

It doesn't necessarily have to come from Buckingham.

Q Did I understand you to say at the end of the year?

A Yes.

Q Is that tax savings on inventory writeoff something that occurred at the end of 1971?

A It occurred as far as their records, yes.

Q And you have it in a schedule that purports to show figures as between May 31, '68 and May 31, '71?

A Yes, sir.

MR. SILVERMAN: If your Honor please, I will move to strike the exhibit.

THE COURT: Well, there certainly seems to be a few questionable items on Page 2, am I right?

MR. SILVERMAN: I would say so, sir.

THE COURT: Am I right, Mr. Odell?

MR. ODELL: I'm not prepared to say they are questionable items. I don't think Mr. Gardner is now in a position to say whether or not they are questionable.

THE COURT: All right.

Maybe by the time he resumes the stand, he may be, so I will at this point strike the exhibit from evidence

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and we will recess until you gentlemen are summoned by a telephone call from the Court.

xxx (Plaintiffs' Exhibit No. 148 was stricken from evidence.)

(Adjournment taken)